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No. 10-695

In The
Supreme Court of the United States

MARK D. LAY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

Petition For A Writ Of Certiorari To The United States Court of Appeals For The Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI
with Appendix

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November, 2010

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QUESTIONS PRESENTED

1. Do investment advisers to hedge funds owe fiduciary duties to investors in the funds?

2. Can the offenses of mail and wire fraud be committed in circumstances where there is no "gain" of any nature to the defendant nor use of the mail or wires to cause a person to part with money or property?

3. Was it reversible error for the trial court to fail to give a proper limiting instruction to the jury in connection with the use at Petitioner's trial of transcript testimony from an earlier deposition?

PARTIES

Petitioner, Mark D. Lay, was defendant in the trial court. Mr. Lay, a registered investment adviser, was convicted under federal mail and wire fraud and investment adviser fraud statutes for losses experienced by a hedge fund he managed, MDL Active Duration Fund (hereinafter "ADF"), into which the Ohio Bureau of Worker's Compensation (hereinafter "OBWC") unlawfully invested and lost $216,000,000.00[1]. There were no allegations that Petitioner profited financially or personally benefited from these losses. This appeal is about losses in the bond market. There was no theft, embezzlement or other gain to Petitioner.

Respondent is the United States of America.

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[1]The evidence at trial indicated that OBWC did not obtain authority to invest into hedge funds until 2004, a point in time subsequent to the initial investments here. OBWC invested $100M on August 20, 2003 and a second $100M on May 21, 2004. Hedge Fund investments were not approved by the OBWC Oversight Commission until August 2004.

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MARK D. LAY,
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UNITED STATES OF AMERICA,
RESPONDENT.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI

Mark D. Lay respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

May 13, 2008 Opinion of United States district court, Northern District of Ohio entering judgment on a jury verdict against Mr. Lay.

July 11, 2008 Amended Judgment of United States district court, Northern District of Ohio.

July 14, 2010 Opinion of United States Court of Appeals for the Sixth Circuit affirming district court.

August 25, 2010 Order of United States Court of Appeals for the Sixth Circuit denying rehearing.

JURISDICTION

The judgment of the Sixth Circuit was entered on July 14, 2010. A Petition for the Rehearing and Rehearing En Banc was denied on August 25, 2010.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

STATUTES CITED TO IN PETITION:

15 U.S.C. §80b-6

15 U.S.C. §80b-1 et seq.

18 U.S.C. §1341

STATEMENT OF THE CASE

A. STATEMENT OF FACTS

This appeal arises from an unprecedented and stunning departure from established judicial precedent in relation to the regulation and prosecution of hedge fund investment advisers. The United States Security and Exchange Commission has defined a hedge fund as any pooled investment vehicle that is privately organized, administered by professional investment managers and not widely available to the public. *See*, Staff Report to the United States Securities and Exchange Commission

"Implications of the Growth of Hedge Funds (September 2003/"SEC Staff Report" at p. 3.").

This is an appeal from the conviction and sentence of Petitioner, Mark D. Lay, an African American, graduate of Columbia University, relating to his management of a hedge fund, in which the Ohio Bureau of Worker's Compensation (hereinafter referred to as "Bureau" or "OBWC") was an investor. Initially, on June 14, 2007, the government filed a four court indictment against Petitioner related to his involvement and/or his company's involvement with the Bureau and investments made by the Bureau into the MDL Active Duration Fund (hereinafter referred to as "ADF"), a hedge fund managed by Lay's company.

The following factual background details the specifics of the relationship between Petitioner and the Bureau. The Bureau or OBWC is an Ohio state agency that assists employers with expenses related to workplace injuries by providing medical and compensation benefits. The Ohio workers' compensation system is the largest exclusive state insurance fund in the United States, with assets of $14 billion and annual insurance premiums and assessments of $2.3 billion. OBWC exercises fiduciary authority with respect to the Ohio State

Insurance Fund (OSIF). This fund is held for the benefit of injured workers and employers of Ohio. OBWC invested funds into ADF on three discrete occasions, one hundred million dollars on August 20, 2003, one hundred million dollars on May 21, 2004 and twenty five million dollars on September 23, 2004. These are the only times OBWC "parted" with property at the behest of Petitioner, that is, it was on these three discrete occasions when funds left OBWC's custodial bank and were transferred to ADF. Other than these three occasions, OBWC did not part with money or property in connection with ADF by reason of any act of Petitioner.

Petitioner founded MDL Capital Management, Inc., (hereinafter referred to as "MDL") in 1992 and served as its Chairman, CEO, Principal Shareholder and Chief Investment Strategist. MDL was registered with the Securities and Exchange Commission (hereinafter referred to as the "SEC") as an investment adviser under the Investment Adviser's Act of 1940 hereinafter referred to as ("the Act").

In May of 1998 Petitioner and the OBWC entered into an Investment Management Agreement under which Petitioner would manage the OBWC's Long Fund, and also established MDL Capital, as an

investment adviser to OBWC under the Investment Advisers Act of 1940. OBWC allocated $355 million of its investment portfolio, referred to as the Long Fund, for management by MDL. There were no problems or questions about any conduct with regard to the Long Fund. It is not the Long Fund investment that is at issue in this appeal.

In May of 2002, Petitioner established ADF. ADF was established independently by Petitioner. OBWC did not finance or underwrite the expenses of establishing the ADF hedge fund. What is significant about ADF is that, unlike the Long Fund, as a portfolio managed by Petitioner for OBWC, ADF belongs to a class of investments that is exempt from the SEC regulatory framework applicable to the Long Fund and investments like it. In the case of the Long Fund, OBWC's funds remained in a custodial bank, Petitioner merely determined how to invest those funds. In the case of ADF, OBWC actually removed funds from its custodial bank and transferred them to ADF for investment by ADF. OBWC was merely an investor in ADF. OBWC had not right to control ADF investment strategy. Petitioner was the investment adviser to ADF. Petitioner was not an investment adviser to OBWC as it related to ADF. For this reason, theories of criminality or even civil

liability applicable to Petitioner's management of OBWC nonexempt investments are not necessarily pertinent to exempt investments such as ADF. In the case of ADF, Petitioner was not OBWC's investment adviser, as he was with the Long Fund. In connection with ADF Petitioner was ADF's adviser, OBWC was an investor only.

The regulatory framework respecting hedge funds acknowledges these truths and therefore reflects "Congress's view that certain highly sophisticated investors, [such as OBWC], do not need all of the protections of the Investment Company Act for the reason those Investors are in a position to appreciate the risks associated with pooled investment vehicles." *See*, S. Rep. No. 293, 104th Cong., 2d Sess. 10 (1996). "Generally, these investors can evaluate on their own behalf matters such as the level of a fund's management fees, governance provisions, transactions with affiliates, investment risks, leverage and redemption rights." *Id.* (Emphasis added). By entering into the hedge fund investment environment, OBWC accepted this risk. The decision by OBWC to invest in ADF was an overlay strategy.[2]

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2 ADF was part of an overall investment strategy being pursued by OBWC. It was part of what is called an "overlay strategy." An "overlay strategy" is an

The jury found that Petitioner, in violation of his fiduciary obligations under the 1940 Act, committed investment adviser fraud against OBWC by managing ADF in a manner inconsistent with leverage guidelines set forth within a private placement memorandum that outlined the terms and conditions of the ADF investments (hereinafter the "PPM"). Specifically, the government alleged that Mr. Lay exceeded guidelines set forth within the pertinent PPM by causing more than 150% of ADF's assets to be leveraged in connection with trades directed by Petitioner. The government alleged that mailing trade confirmation slips detailing these trades, although containing no false information, was mail fraud. As stated above, Petitioner was not an investment adviser for OBWC as to the ADF hedge fund. He was investment adviser to ADF. OBWC was merely an investor in ADF. According to the relevant PPM:

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investment strategy which is "overlaid" on top of existing strategies, and does not disturb existing investments. Overlay strategies can take many forms, such as currency overlays, interest rate overlays, cash management overlays, and many other types.

> The Fund is expected to leverage the Fund's investment portfolio as a means to increase yield and enhance total return. Up to 150% of the Fund's assets, at the time of investment, may be leveraged (*i.e.*, the combined value of borrowings and short positions). Leveraging will include, but is not limited to, short selling of securities, reverse repurchase agreements, certain option and futures transactions plus any borrowings to leverage the Fund's assets. Although the use of leverage may enhance returns on the Fund's portfolio and increase the number of investments that may be made by the Fund, it may also substantially increase the risk of loss. The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.

PPM at 3. (Emphasis added)

1. DURATION AND LEVERAGE

In the context of this appeal the issue of leverage is central. "Leverage means that the return on an owner's equity in a leveraged investment is not equal to the return on the investment, because the investment is not financed entirely with the owner's

money. For example, the owners fund may put up $1 billion of their own money, borrow $9 billion, and buy $10 billion in market value of Treasury bonds. The owners' equity (*i.e.*, the net asset value, or "NAV" of the fund) is $1 billion. One measure of leverage is the ratio of assets to equity, which is 10 in this example. Another measure of leverage is the debt-equity ratio, which is 9 in this example. If the bonds increase in value by 5%, or $0.5 billion, the NAV increases by the same amount (ignoring interest on the borrowing), and the return on equity is 50% (*i.e.*, $0.5 billion/$1 billion). The 50% increase in equity could be calculated by multiplying the asset-equity measure of leverage by the return on the bonds (*i.e.*, 10 x 5%).

Leverage, it is simple calculation that any sophisticated investor such as OBWC could calculate from the reports provided by Petitioner. It quite simply, is the overall position divided by the actual value of the position. Another example would be if a fund had a position of one billion dollars in bonds, but the portfolio had an actual value of 200 million dollars, the leverage would be 5 to 1 or 500%. Leverage will change based on changes to the overall position or changes in the value of the portfolio. Leverage is a calculation that changes from second to

second as the value of the portfolio changes with fluctuations in the market. Even if the actual position does not change, the leverage may change dramatically based on the market. If the value of the portfolio increases, the leverage will decrease and to the contrary if the value of the portfolio decreases, the portfolio leverage will increase. In the case of OBWC, the overlay strategy was to protect the portfolio against higher interest rates. The overlay strategy is a one way bet. It is not a strategy that capitalizes on various changes in the market. In this case, interest rates did not go higher but went lower. As rates went lower the value of the portfolio went down thus increasing the leverage substantially. All changes in leverage are therefore not simply attributable, as the government argued, to acts of Petitioner. Leverage may change simply by reason of market conditions. Here, the ADF portfolio continued to lose money as interest rates went lower. OBWC was aware of this and invested more cash in May 2004 which decreased leverage in ADF so ADF could operate. As ADF, an overlay strategy, lost money, the rest of the OBWC portfolio made money, thus you get the term "hedge". An overlay strategy is just a hedge for the rest of the portfolio. OBWC invested additional capital in ADF on two occasions,

after it was known that money had been lost. These investments are evidence of OBWC's sophistication and their ability to determine the value of the ADF portfolio.

Despite the above, the jury found that Mr. Lay violated Section 80b-6 of the Act, by repeatedly exceeding the above leverage guideline. The superseding Indictment stated by reason of Mr. Lay's fraud and deceit upon the OBWC by using leverage in excess of 150% and not informing OBWC or gaining its consent, OBWC lost $216,000.000 of its $225,000,000 ADF investment. Counts 2, 3 and 4 of which Petitioner was also convicted alleged conspiracy, wire and mail fraud, and aiding and abetting offenses based upon Petitioner's alleged misrepresentations and nondisclosures relating to how much leverage had been utilized in connection with ADF trading. These convictions must be reversed as a matter of law for the reason Petitioner was not OBWC's investment adviser in relation to ADF, OBWC was a sophisticated investor, and there was no use of the mail of wires to cause OBWC to part with money.

B. COURSE OF PROCEEDINGS

The trial for this matter began on October 12, 2007, with the selection of a jury. The trial itself began on October 15, 2007. The trial concluded with guilty verdicts returned by the jury on October 30, 2007, to investment advisory fraud, mail and wire fraud, conspiracy to commit or attempt mail and wire fraud, and aiding abetting. In addition, the jury returned a verdict regarding the issue of forfeiture, finding that the proceeds that were obtained and subject to forfeiture constituted the sum of $590,526.23 and $212,967,084.76 in restitution.

Following the conviction, Petitioner was released on bond pending sentencing. Petitioner filed a Motion for Acquittal, or in the alternative, a Motion for a New Trial, on November 13. 2007. After the government's response and oral argument on May 5, 2008, the District Court entered a Memorandum Opinion and Order on May 13, 2008, (R.158) denying Lay's motions.

A sentencing hearing was held on July 3, 2008 and July 8, 2008. A judgment was thereafter entered and on July 9, 2008, Lay was sentenced to 60 months as to Count 1 and 144 months as to each of counts 2, 3 and 4.

Petitioner appealed the decision of the District Court. Timely appeal was filed in the Sixth Circuit.

REASON FOR GRANTING THE PETITION

THE SIXTH CIRCUITS FAILURE TO FOLLOW GOLDSTEIN HAS CREATED A CONFLICT BETWEEN THE COURTS

a. Investment Adviser's Act and Goldstein

Federal law determines whether a fiduciary relationship exists in relationships governed by the Investment Advisor's Act. Specifically, Section 206 of that Act governs whether a fiduciary duty is owed from an investment adviser, or adviser to a ADF Hedge Fund, to their 'client.' *Goldstein v. SEC*, 451 F. 3d 873, 881 (D.C. Cir. 2006); see also *SEC v. Trabluse*, 526 F. Supp.2d 1008 (N.D. Cal. 2007)(stating that with respect to the Investment Adviser's Act of 1940, the Securities and Exchange Commission must show a breach of fiduciary duty to the fund itself since the adviser owes a duty only to the fund and not the fund's investors). Also see, *SEC v. North Shore Asset Management*, 2008 U.S. Dist. LEXIS 36160 (S.D. NY May 5, 2008) (SEC can not bring actions against hedge fund advisers where

investments are defrauded). Specifically, "*U.S.C.S. §. 80b-1 et seq.*, makes it unlawful for any investment adviser, registered or not, to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." *Goldstein*, 451 F.3d at 881. Additionally, "The United States Supreme Court has held that 12 U.S.C.S. § 80b-6(2) created a fiduciary duty of loyalty between an adviser and his client which required the adviser to disclose self interested transactions to him." *See SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 191-92 (1963).

An accurate understanding of the *Goldstein* case is pivotal to this appeal. Therein, the D.C. Circuit court stated that it was "counterintuitive" to characterize the investors in a ADF Hedge Fund as the "clients" of the adviser. *Goldstein*, 451 F.3d at 881. The adviser owes a fiduciary duty only to the fund itself, not to the fund's investors. *Goldstein* further states that Congress did not intend "shareholders, limited partners, or beneficiaries" of a ADF Hedge Fund to be counted as "clients." Id. At 879. Here there was no investment adviser's agreement between Petitioner and OBWC as to ADF. There was a specific exclusive investment adviser's

agreement between ADF and Petitioner of which OBWC was aware.

The fund manager -- the adviser -- controls the disposition of the pool of capital in the fund. The adviser does not tell the investor how to spend his money; the investor made that decision when he invested in the fund. *Id.* at 880. Having bought into the fund, the investor fades into the background. *Id.* His role has become completely passive. *Id.* If the person or entity controlling the fund is not an "investment adviser" to each individual investor, then a *fortiori* each investor cannot be a "client" of that person or entity. *Id.* In *Goldstein*, the court states that the "kind of fiduciary relationship the Act was designed to regulate is the "type of direct relationship [that] exists between the adviser and the fund, but not between the adviser and the investors in the fund." *Id.*

The Courts below correctly analyzed and cited to Goldstein, and recognized that *Goldstein* concluded that "hedge fund investors are not clients of the fund adviser . . ." The Courts also quoted *Goldstein's* analysis pertaining to the structure of hedge fund relationships. Prior to the SEC's new rule attempting to expand the definition of hedge fund client, the SEC explained that:

> "a 'client of an investment adviser typically is provided with individualized advice that is based on the client's financial situation and investment objectives. In contrast, the investment adviser of an investment company need not consider the individual needs of the company's shareholders when making investment decisions, and thus has no obligation to ensure that each security purchased for the company's portfolio is an appropriate investment for each shareholder.'"

(MOO, Doc, #158, p. 28-9)(quoting *Goldstein*, 451 F.3d at 880, quoting Status of Investment Advisor Programs Under the Investment Company Act of 1940, 62 Fed. Reg. 15, (March 31, 1997)).

The Courts below further correctly quoted *Goldstein's* holding that "hedge fund investors are not client's of the fund's investment adviser" because conflicts of interest would be "inevitable" if the adviser owed a fiduciary duty to "act in the client's best interest, and fully disclose material conflicts the adviser has with his clients, to both the fund and the fund's investors." *Id.* (citing *Goldstein*, 451 F.3d at 881).

The Sixth Circuit correctly observed that the Goldstein court struck down the SEC rule defining ADF Hedge Fund investors as clients because to do so would manipulate the meaning in that "The Commission has, in short, not adequately explained how the relationship between ADF Hedge Fund investors and advisers justifies treating the former as clients of the latter." *Id.* (citing *Goldstein*, 451 F.3d at 882).

Moreover, and truly applicable to the present appeal, the trial Court recognized that the *Goldstein* court did not accept the SEC's argument that different classes of investors should be treated differently because if there are "certain characteristics present in certain investor-advisor relationships that mark a "client" relationship, then the Commission should have identified those characteristics and tailored its rule accordingly." *Id.* (citing *Goldstein*, 451 F.3d at 882-83).

To state it more succinctly, the Circuit Court itself accepted the *Goldstein* ruling that an investor in a hedge fund is not a client of the adviser to the fund. Moreover, the Circuit specifically stated that the lack of a fiduciary relationship between the advisor to the fund and the investors in the fund is not altered by the facts of a particular case, i.e. as a

matter of law, the investors in the fund are not clients of the fund's advisor and no fiduciary duty is owed.

What follows in the District Court's opinion is perplexing, to say the least. Directly contrary to its immediately preceding legal analysis, the District Court stated that "the facts of *Goldstein* . . . are very different than the facts of this case." And went on to find that, based upon the facts of this case, there was a fiduciary duty owed. The District Court held in direct opposition to the case law it cited to support its position. The Sixth Circuit affirmed this erroneous conclusion.

As admitted by the government and the District Court the primary governing document that established the parameters of the business relationship between Mark Lay, the ADF Hedge Fund and the Bureau, is the PPM dated January 15, 2003. In that document, it is abundantly clear that the client was the ADF Hedge Fund, that the Bureau was an investor in the fund and that "the director's principal duty is to act in the best interest of the Company[,]" i. e., the ADF Hedge Fund. (PPM p. 23). Undeniably, Mark Lay's fiduciary responsibilities here were to the ADF Hedge Fund, not OBWC.

As investors, the Bureau was repeatedly advised and encouraged to seek outside counsel to evaluate their involvement with the ADF Hedge Fund. The Bureau was told that they could not reply upon the advice of Mark Lay and MDL, the advisor to the ADF Hedge Fund: "The investors [are] not represented by [the experts to the ADF Hedge Fund.] Each prospective investor should consult his own legal, tax and financial advisers regarding . . . the suitability of an investment in the [Hedge] Fund." (PPM p. 23). The Bureau is never referred to as a client in the PPM. Moreover, it is obvious from a comprehensive reading of the PPM that one of its primary purposes is to establish the arms length relationship between *investors* in the ADF Hedge Fund and the advisers to the ADF Hedge Fund.

It is beyond dispute that the Sixth Circuit erred in failing to find that, as a matter of law, the Bureau was not the client of MDL as the adviser to the ADF Hedge Fund. *Goldstein* makes is clear that due to the reality of the ADF Hedge Fund investment vehicle and the manner in which it must be administered, it is counterintuitive that the Bureau was a client.

b. Fiduciary Relationship

A fiduciary relationship can only be created when both parties understand that a special trust or confidence has been reposed. *Aschinger v. Columbus Showcase Co.*, 934 F.2d 1402, 1408 (6th Cir. 1991). Such a relationship cannot be predicated on one party's allegedly superior knowledge of the facts of a particular transaction when the relevant facts are readily available to both parties. *Id.* at 1408.

The PPM repeated, over and over again, that the investors were to seek outside counsel and advice from its own financial advisor before even entering into the agreement as well as when deciding if and how much to invest in the ADF Hedge Fund.

Moreover, the PPM virtually screams to potential investors that the ADF Hedge Fund is an extremely risky investment. Potential investors are warned, cautioned and advised of all material facts that may affect their investment, including the risk that their total investment may be lost. Potential investors are warned cautioned and advised to seek outside consultation before choosing to invest. The PPM states:

> There is a high degree of risk associated with an investment in the Fund and an investment in the Fund should only be

> made after consultation with independent qualified sources of investment and tax advice.

(PPM, p. 17).

As to risks, the PPM states again, also in all capital letters:

> THE SHARES ARE SPECULATIVE AND INVOLVE A HIGH DEGREE OF RISK. THEY ARE SUITABLE ONLY FOR PERSONS WHO CAN AFFORD TO LOSE THEIR ENTIRE INVESTMENT. SHAREHOLDERS SHOULD READ THE MEMORANDUM AND ARTICLES OF ASSOCIATION AS WELL AS THE FUND'S CONTRACTS WITH SERVICE PROVIDERS WHICH ARE REFERENCED IN "STATUTORY AND GENERAL INFORMATION."

(PPM, p. 24)(emphasis in original).

On September 10, 2008, the SEC amended its rules for enforcement actions under §80b-6, the statute under which Mr. Lay was prosecuted, in response to the opinion in *Goldstein v. SEC*, 451 F. 3d 873 (D.C. Cir. 2006). While *Goldstein* is not

binding authority in the Sixth Circuit, the interpretation of the SEC concerning the operation of §80b-6 is entitled to great deference from a federal court. *United States v. Mead*, 533 U.S. 218 (2001) and *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The Sixth Circuit attempted to distinguish *Goldstein* by stating it does not stand for the proposition that an investor may never be the client. This is exactly what Goldstein says is never possible. In point of fact, *Goldstein* states:

> An investor in a private fund may benefit from the adviser's advice (or he may suffer from it) but he does not receive the advice *directly*. He invests a portion of his assets in the fund. The fund manager-the advisor-controls the disposition of the pool of capital in the fund. The adviser does not tell the investor how to spend his money; the investor made that decision when he invested in the fund. Having bought into the fund, the investor fades into the background; his role is completely passive. If the person or entity controlling the fund is not an "investment adviser" to each individual investor, then a *fortiori* each investor cannot be a "client" of that person or

entity. These are just two sides of the same coin.

* * *

If the investors are owed a fiduciary duty and the entity is also owed a fiduciary duty, then the adviser will inevitably face conflicts of interest. Consider an investment adviser to a hedge fund that is bankrupt. His advice to the fund will likely include any and all measures to remain solvent. His advice to an investor in the fund, however, would likely be to sell. For the same reason, we do not ordinarily deem the shareholders in a corporation the "clients" of the corporation's lawyers or accountants. *see* RESTATEMENT, *supra*, §96 cmt. b ("By representing the organization, a lawyer does not thereby also form a client-lawyer relationship with all or any individuals. . . who have an ownership or other beneficial interest in it, suck as its shareholders."). While the shareholders may benefit from the professionals' counsel indirectly, their individual interests easily can be drawn into conflict with the interest of the entity. It simply cannot be the case that investment advisers are the servants of two masters in this way.

Goldstein, pp. 11-12, 15. (Emphasis in the original and emphasis added)

Under the *Chevron* doctrine it was determined that a federal court should defer to an agency's interpretation of a statute if the agency's interpretation is reasonable or permissible and the statute is ambiguous or there is a gap that Congress intended the agency to fill.

When the *Chevron* rule is applied here, you have the SEC revisiting its rules concerning the reach of §80b-6 in response to an opinion, *Goldstein*, that states unequivocally - hedge fund investors can never be clients of the investment advisor, and point two - a point the United States has failed to address, investment advisors owe no fiduciary duties to hedge fund investors. In point of fact, SEC FL. Release No. IA-2628; File No 57-25-06 states in p. 13: "206(4)-8 does not create under the Advisors Act a fiduciary duty to investors or prospective investors in a pooled investment vehicle not otherwise imposed by law." *Goldstein* stated unequivocally, prior to passage of this new rule, that advisors did not owe investors any fiduciary duties. As such there were no other fiduciary duties imposed by law.

Here, the prosecution under §80b(6)(1) and (2) depended on a requirement to find the OBWC was

Petitioner's client, in relation not the ADF, a status that was determined as a matter of law in *Goldstein* not to exist. The prosecution under §80b-6(4), the catchall, depended on a requirement that the jury find that Petitioner was an investment adviser to OBWC and owed fiduciary duties to the OBWC in relation to the ADF, duties which *Goldstein* stated that advisors do not owe. The SEC rule was amended to clarify that a new provision Rule 206(4)-8 would delineate that conduct required under §80b-6 as it relates to investors or prospective investors. Section 80b-6 in its entirety is only applicable to investment advisers in relation not the relevant investment here, ADF, Petitioner was not OBWC's adviser, so 80b-6 has no applicability at all.

ADF had a separate and distinct relationship with Petitioner. There is some question whether OBWC was even authorized to invest into ADF or any other hedge fund. The OBWC policy authorizing alternative investments was not approved until 2004, after the initial investments here.

ADF was intended to receive the investment of the OBWC and potentially other investors as well. The fact the OBWC ended up as the sole investor in ADF, does not change OBWC's status as merely an investor.

It was common knowledge now and at the time this fund was created that a hedge fund is a high risk investment vehicle. That is why it is limited to sophisticated investors. Concomitant with the potential for high gains is the risk of substantial losses, including the total loss of the investment. (PPM p. 24). It is for this reason that a different set of rules and regulations apply to hedge funds. These rules and risks were fully described and outlined in the PPM, the documentation that governed the subject of ADF Hedge Fund and that delineated the terms of the agreement between the OBWC, the ADF Hedge Fund, MDL and Mark Lay. By entering into the agreement, OBWC accepted these terms and these risks. Pursuant to the agreement, OBWC chose to accept the lack of fiduciary relationship and the risks and potential for a total loss of its investment due to unforeseen volatility of the market.

1. ADF Hedge Fund Established as the Client of MDL and OBWC Established as an investor in the ADF Hedge Fund: Fiduciary Duty Owed to the ADF Hedge Fund as a Whole and Did Not Extend to Individual Investors.

OBWC specifically, unambiguously and unequivocally accepted that the ADF Hedge Fund was the client of MDL. OBWC accepted that it was an *investor* only in the ADF Hedge Fund, and that it was not a *client* of Mark Lay with respect to the ADF Hedge Fund. (PPM, p. 18). An investor in an ADF Hedge Fund is not the same thing as a client of the ADF Hedge Fund. Mark Lay's obligation with respect to the ADF Hedge Fund was to make investments that profited the fund, not the individual investors in the ADF Hedge Fund. (PPM, p. 18)

That OBWC is an investor in the ADF Hedge Fund and not a client is reiterated throughout the PPM. Any investor in the ADF Hedge Fund, including the OBWC, was advised to seek outside advice and counsel before entering into the agreement. Potential investors were specifically told not to rely upon the investment adviser to the ADF Hedge Fund, MDL, nor the ADF Hedge Fund's or Investment Adviser's experts, but were to seek their own investment advice and their own independent expert advice. The Sixth Circuit Opinion creates a relationship that was expressly negated by the relevant transaction documents.

Several specific examples of this exist in the PPM. At the outset of the PPM, it is stated, in all capital letters:

> PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE REGISTRATIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY DOUBT ABOUT THE CONTENTS OF THIS MEMORANDUM, YOU SHOULD CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

(PPM, p. ii).

In the body of the PPM, it is stated:

> *Lack of Independent Experts Representing Investors.* The Fund and the Investment Adviser have each

> consulted with counsel, accountants and other experts regarding the formation and terms of the Fund and the Advisory Agreement. The investors, however, have not been represented by such independent experts. Each prospective investor should consult his own legal, tax and financial advisers regarding the desirability of purchasing shares and the suitability of an investment in the Fund. Foley and Lardner and Appelby, Spurling & Kempe are a U.S. and Bermuda counsel to the Fund, respectively, and do not represent the prospective investors or shareholders of the Fund.

(PPM, p. 23). (emphasis in the original).

Also stated clearly and unambiguously was that the ADF Hedge Fund would be managed by a Board of Directors, which would have absolute discretion as to when and how to invest. The Board consisted of Mark. D. Lay, Steven L. Sanders, and Edward Adatepe, who were the principals of MDL and Oskar P. Lewnowski and Raymond Morrison of Olympia Capital International Inc., which was the Fund's administrator (PPM, p. 18). The PPM further states that the investments made on behalf of the

ADF Hedge Fund would be determined by the Board and that "The Investment Adviser, in its sole and absolute discretion and authority as an investment adviser to the fund will ultimately identify and select investments for the Fund." (PPM, p. iv). (Emphasis in the original).

2. Percentage of Assets Permitted to be Leveraged Within Sole Discretion of Hedge Fund Board of Directors.

A highly critical fact to appreciate for this appeal is the percentage of assets the OBWC agreed that the ADF Hedge Fund Board and Mark Lay could leverage. The PPM, the primary governing document for the agreement between the OBWC and MDL, states that the leverage *guideline* is up to 150% of the Fund's assets at the time of investment. (PPM, p. 3). This figure is a *guideline*. It is not a limitation and it is not a prohibition, it is a "guideline".[3]

---

[3]Note in the case of Long Term Capital Management, a 100 billion dollar hedge fund established in 1994 by John Meriwether Vice Chair, now a head of bond trading at Saloman Brothers, at the time of the 1998 collapse the funds assets had been over leveraged 250-1. LTCM's collapse threatened the stability of the entire American market. There were no criminal prosecutions. See,

It is indisputable that the PPM grants the Board of Directors absolute and sole discretion to exceed the guideline when it determines that it is in the best interest of the ADF Hedge Fund to do so. This fact is acknowledged by Terry Gasper, the Chief Financial Officer of the OBWC. Terry Gasper testified that he understood the PPM to give the Board of Directors the sole discretion to change the guideline, and that they could do so at any time, without notice. (Testimony T.C. Gasper, Doc. #102, pp. 134-135). In addition, the PPM, which was signed by the officers of the OBWC, states:

> **The percentage included above is intended as a guideline as may be changed from time to time at the sole discretion of the Board of Directors.**

(PPM, p. 3). (emphasis added)

The grant of authority to Mark Lay, as to the ADF Hedge Fund, could not be clearer.

3. Risk Factors and all Relevant Facts Explained and Agreed Upon By OBWC

Lowenstein, Roger (2000) "When Genius Failed: The Rise and Fall of Long-Term Capital Management"", Random House.

In the PPM, MDL went to great lengths to explain the risk factors of the ADF Hedge Fund in unambiguous terms. For example, at the very beginning of the PPM it is stated in bold capital letters:

> **THE PURCHASE OF SHARES IS SPECULATIVE AND INVOLVES A HIGH DEGREE OF RISK, THERE IS NO ASSURANCE THAT THE FUND WILL BE PROFITABLE. SEE THE SECTION ENTITLED "RISK FACTORS" WITHIN THIS MEMORANDUM FOR A DESCRIPTION OF CERTAIN RISKS INVOLVED IN THE PURCHASE OF SHARES.**

(PPM, p. iii) (Emphasis in the original).

Specifically as to the risks of leverage, the PPM states that is the 150% guideline is not enough to cover a decline in value, additional collateral may be required:

> Risks of Leverage. If the Fund's assets decline in value or there are significant redemptions from the Fund, the Fund may be required to post additional

> collateral with the lender or liquidate assets to pay off its borrowings. Moreover, if the assets under management are not sufficient to pay the principal of and interest on the debt when due, the Fund could sustain a total loss of its investment.

(PPM, p. 19).

It is important to reiterate here that the PPM was ambiguous that:

> **The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.**

(PPM, p. 3). (Emphasis added.)

The PPM further makes clear to those who chose to invest in the ADF hedge Fund that there is a potential for conflicts of interests to arise between the fund and other clients of MDL. (PPM, p. 16). By agreeing to the terms of the PPM, the investors in the ADF Hedge Fund accepted the potential that the investment adviser may engage in transactions or investments for its own account or the account of any other client, that may not benefit the ADF Hedge

Fund, but if they do so invest, it shall be in good faith and on a fair and equitable basis. (PPM, p. 17).

The OBWC anticipated, as did many others, that if long term interest rates had increased in 2003-2004, the ADF Hedge Fund would have been highly successful. However, long term interest rates did not rise and losses were sustained due to the unexpected events in the markets. There was absolutely no gain to Mr. Lay.

In *Goldstein*, the Court discussed at length the distinction between an investor and a client in the context of hedge funds. "At best it is counterintuitive to characterize the investors in a hedge fund as the client of the adviser's. *Id* at 883. Citing *Am. Bar Ass'n v. FTC*, 368 U.S. App. D.C. 368, 430 F.3d 457 (D.C. Cir. 2005). (Emphasis added.)

The Sixth Circuit Opinion does exactly what *Goldstein* points out as counterintuitive, states contrary to *Goldstein's* prohibition, that an investment advisor may indeed serve two masters, the investor and the client.

c. Wire Fraud and Mail Fraud

The evidence did not establish that Mr. Lay was guilty of either mail or wire fraud, aiding and abetting, or a conspiracy to commit either. This

assertion is true as a matter or law, for the reason there was no evidence at all that money or property was obtained through a material misrepresentation or that the mail or wires were used in furtherance of a scheme to obtain money or property. OBWC parted with property voluntarily on three occasions, when it invested in ADF, not when the trades directed by Petitioner occurred. This is a fatal defect in this prosecution.

The Sixth Circuit has stated: "mail fraud cases may be used to analyze wire fraud cases." *United States v. Daniel*, 329 F.3d 480, 487 (6th Cir. 2003).

> The Supreme Court construed the statute to "include[e] everything designed to defraud by representations as to the [*15] past or present, or suggestions and promises as to the future." *Neder*, 527 U.S. at 24 (quoting *Durland, 161 U.S. at 313*). Accordingly, the Court held that materiality of falsehood is an element of the federal mail fraud, wire fraud, and bank fraud statutes. *Neder, 527, U.S. at 25.*
>
> In general, a false statement "is material if it has 'a natural tendency to

> influence, or [is] capable of influencing, the decision of the decision-making body to which it was addressed.'" *Id. at 16* (*quoting United States v. Gauding, 515 U.S. 506, 509, 115 S. Ct. 2310, 132 L.Ed. 2d 444 (1995)*). The misrepresentation or omission must have th purpose of inducing the victim of the fraud to part with property or undertake some action that he would not otherwise do absent the misrepresentation or omission. *United States v. Daniel*, 329 F. 3d 480, 487 (6th Cir. 2003).

United States v. Birnic, 193 Fed Appx. 528, 534, (6th Cir.2003).

First with respect to materiality, "It is clear that as an element of the "scheme or artifice to defraud "requirement, the government must prove that the defendant said something materially false." *Daniel* at 486. There was no evidence of Mr. Lay uttering a false statement related to ADF that caused OBWC to part with money and sending it by wire or mail.

Here the government alluded on pp. 13-16 in the Superseding Indictment to trade confirmation statements. These confirmation statements do not contain false information. What's more, in cases

where mailing trade confirmation statements constituted a violation of 18 U.S.C. §1341, the statements were transmitted for the purposes of executing the artifice or scheme. *See, United States v. Marando*, 504 F.2d 126(2d Cir. 1974) where trade confirmation slips were mailed and determined to be an integral part of a scheme to *obtain* property; *also see, United States v. Grossman*, 843 F.2d 78 (2d. Cir. 1988) where it was determined that:

> The mailings of the confirmation slips did further the purpose of executing the scheme. The confirmation slips (1) notified the relatives that the purchase or sale actually had been completed; (2) provided an on-going tally of purchases, allowing the relatives to cover each other's positions; (3) concealed the fraud by maintaining an appearance of normality, *see United States v. Cohen, 518 F.2d 727, 737 (2 Cir.), cert. denied, 423 U.S. 926, 46 L. Ed. 2d 252 (1975)*; and (4) allowed the relatives to demonstrate ownership after the recapitalization announcement. *Pereira v. United States, 346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954)*. [**27]

To establish a violation of the mail fraud statute, "the mailing must be for the purposes of executing the scheme." *United States v. Maze*, 414

U.S. 395 (1974). To state an offense under 18 U.S.C. §1341 the Supreme Court determined in *Cleveland v. United States*, 531 U.S. 12 (2000) that the Indictment must allege that the defendant not only devised a scheme or artifice, but also used that scheme or artifice to obtain money or property. *See, United States v.Males*, 459 F. 3d 154 (2d Cir. 2006) (Emphasis added). Here the Indictment states ADF received its first $100,000,000.00 before Mr. Lay ever executed a trade. At best the allegations here establish that having lawfully obtained property, Mr. Lay abused the property by investing it in a manner inconsistent with PPM guidelines. The mail was not used to obtain money or property here. There are no facts alleged that indicate that property or money was obtained through a scheme that involved a use of the mail. The trade confirmation slips here unlike in Grossman or Mirando did not contain false information, did not document illegal insider trades, and were not transmitted to obtain money or property. The alleged nondisclosures and misrepresentations concerning leverage alleged in the Indictment are not related to the mailing of confirmation slips. The trades reflected on the listed slips were lawful trades for a hedge fund. It does not matter that OBWC did not authorize them, the PPM

gave ADF's board sole discretion to deviate from the leverage guideline not OBWC. The trade confirmation statements report the purchases of bonds on a certain date, from a certain broker, at a certain price. All of this information is true. On these facts a violation of 18 U.S.C. §1341 was not established.

If the jury believed that the scheme or artifice to defraud was the initiation of trades by Mr. Lay utilizing excess leverage, employing excess leverage is not a misrepresentation for the purpose of inducing a victim to part with property. The facts here establish OBWC invested funds in ADF on three discrete dates, August 20, 2003, May 21, 2004 and September 23, 2004. These are the only times OBWC "parted" with property. The Indictment does not focus on these events. This is contrary to well established Sixth Circuit authority. In point of fact:

> "Mail fraud consists of (1) a scheme or artifice to defraud; (2) use of mails in furtherance of the scheme; and (3) intent to deprive the victim of money or property." *United States v. Turner, 465 F.3d 667, 680 (6th Cir. 2006).* Materiality of falsehood is a requisite element of mail fraud. Neder *v. United States, 527 U.S. 1, 25, 119 S. Ct. 1827,*

> *144 L. Ed. 2d 35 (1999)* The misrepresentation "must have the purpose of inducing [*7} the victim of the fraud to part with the property or undertake some action that he would not otherwise do absent the misrepresentation or omission." *United States v. Daniel, 329, F.3d 480, 487 (6th Cir. 2003).* A misrepresentation "is material if it has a natural tendency to influence, or is capable of influencing, the decision of the decision-making body to which it was addressed." *Neder*, 527 U.S. at 16 (internal citation and quotation marks omitted).

McCauliff, supra.

There was no evidence here that the OBWC parted with property by reason of a material misrepresentation.

> The mail fraud stated "does not purport to reach all frauds, but only those limited instances in which the use of the mails is part of the execution of the fraud." *Kann v. United States*, 323 U.S. 88, 95, 89 L.Ed. 88, 65 S. Ct. 148 (1944). Accordingly, the government must show beyond a reasonable doubt that [defendant] caused the mailings listed

> in the indictment to be sent and that the mailings were in furtherance of the fraud.

United States v. Pimental, 236 F. Supp. 2d 99 (D.C. Mass 2002).

Here there was no proof of any mailings in further of a scheme to exceed leverage or that the OBWC parted with money due to a mailing. The same deficit applies to Counts 3 and 4.

d. The Sixth Circuit Failed To Follow Skilling

Aside from the above, on June 24, 2010, the United States Supreme Court in *Skilling v. United States*, 561 U.S. _____ (2010), No. 08-1394, announced a seismic shift in mail fraud prosecutions. The Sixth Circuit totally ignored the *Skilling* opinion.

The *Skilling* opinion highlights what the government's burden of proof is in a prosecution under 28 U.S.C. § 1341 for mail fraud, one of the offenses that Mr. Lay is charged with here. *Skilling* makes it clear that an essential element in a mail fraud prosecution is evidence of some form of gain or enrichment to the defendant. In point of fact, *Skilling* states:

> Enacted in 1872, the original mail-fraud provision, the predecessor of the

> modern-day mail- and wire-fraud laws, proscribed, without further elaboration, use of the mails to advance 'any scheme or artifice to defraud.' *See, McNally v. United States*, 483 U. S. 350, 356 (1987). In 1909, Congress amended the statute to prohibit, as it does today, 'any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises.' §1341 (emphasis added); see id., at 357-358. Emphasizing Congress' disjunctive phrasing, the Courts of Appeals, one after the other, interpreted the term "scheme or artifice to defraud" to include deprivations not only of money or property, but also of intangible rights.

Id. (emphasis added) *Skilling* goes on to discuss the elements of a honest services fraud claim versus other frauds. The Court focuses on the requirement for symmetry, in a standard mail fraud case, that is "the victim's loss of money or property supplied the defendant's gain, with one the mirror image of the other.' *Id.*

In this case it is undisputed that Petitioner did not realize any gain as a result of an alleged misuse of the mails. The victim, the Ohio Bureau of Workers

Compensation (OBWC), losses were due to unsuccessful attempts by Petitioner to recoup losses through increased use of leverage. In some instances gains resulted from the use of increased leverage. In other instances losses occurred from its use. In no instance, however, did Petitioner realize any money or property from the use of allegedly excessive leverage. In most instances leverage changed due to market fluctuations, not Petitioner's acts.

Petitioner received no compensation from OBWC by reason of trading activity or volume. All of Petitioner's fees were paid by the Active Duration Fund (ADF), not the OBWC. Mr. Lay received no compensation from OBWC for ADF trades or managing OBWC funds.

The absence of any gain of any nature by a defendant is fatal to a mail fraud prosecution. *Skilling* emphasizes this point.

The use of excessive leverage was not a scheme to defraud. It was an investment strategy that failed. The purpose and intent of the strategy was not of a nature that will support a mail fraud prosecution. *See, Skilling (citing, United States v. Bloom*, 149 F. 3d. 649, 655 (7th Cir. 1998) and *United States v. Panarella*, 277 F.3d 678, 692 (3rd Cir. 2002) (requires that a defendant act in pursuit of private gain)).

Skilling determined that a 28 U.S.C. § 1346 prosecution requires as "offense conduct" evidence of either bribery or kickbacks and that the ambit of a criminal statute should be resolved in favor of lenity. *Rewis v. United States*, 401 U.S. 808 (1971). The "offense conduct" in Petitioner's case, a 28 U.S.C. § 1341 prosecution, according to *Skilling*, the conduct must include an element of gain at the expense of a victim, here OBWC.

In this case the gain element is totally lacking. In point of fact, the District Court states at p. 23 of Petitioner's sentencing memorandum. Case no. 1:07 CR-00339- DOD:

> As the Court undertakes a study as to the seriousness of the offense and the need to impose the sentence that promotes respect for the law and provides just punishment for the defendant's conduct, the defendant's sentencing memorandum reviewing the defendant's past history including his past business, is relevant. The defendant recites the fact that he opened his business known as MDL Capital in 1994 beginning only with a telephone and receptionist and built the business into a highly successful venture, employing over 40 people. His

counsel contends that he 'became one of the nations better recognized financial commentators, appearing regularly on MSNBC and on business related shows. His opinions were reflected frequently in the Wall Street Journal. He was selected as the Entrepreneur of the Year in Pittsburg by the accounting firm of Ernst & Young.' Continuing, his counsel recite the fact that the Long Fund (or the Core Fund) made money as did the state of Ohio generally. His counsel contend 'the fact is that the circumstances of the market developed in a way never before experienced. Looking back in hindsight, as the Court can do, *it seems obvious that he should have stopped following the investment strategy he had in place. But at the time, no one had ever seen an instance in which rising bond prices would not lead to a devaluation of existing bonds.* But that is precisely what happened in this time frame. *It was the first time in economic history of the United States that that occurred*, and his strategy failed, and because of the leverage, failed dramatically.'

* * *

It seems apparent that the defendant had not lost any monies for any clients

> in the management of the MDL investments until the defendant began excessive over-leveraging with the ADF. It appears from his past experiences with Mellon Bank and PNC that it was not the first time defendant took great risks in the belief that he could recoup his losses. The Court notes that the defendant, born in 1963, actively pursued a good education and did not demonstrate criminal tendencies. The defendant has no criminal record. The defendant appears to have been a responsible father. *It does not appear to the Court that the defendant was motivated to gain more income by his management of the ADF.*

Id. (emphasis added)

As the District Judge indicated, there was no evidence whatsoever that the mails were used by Petitioner in any scheme to defraud another or to generate gain for Mr. Lay. *Skilling* makes it clear the absence of this element is fatal to a mail fraud prosecution. The mailing of trade confirmation slips by third parties that document specific transactions, did not result in any gain or benefit to Mr. Lay.

Aside from the clarification provided by *Skilling* in relation to mail fraud prosecutions, Skilling also explains that Constitutional error occurs

where a jury is instructed on alternative theories of guilt and returns a general verdict that may rest on a legally invalid theory.

In this case, the jury was instructed in connection with each of the four counts on alternative theories of liability. In each instance here, the jury was permitted to find that Petitioner was an investment adviser without any requirement to also determine whether he was an investment adviser to the alleged victim, or whether the victim was an investor as distinguished from Mr. Lay's client. The jury was also permitted to determine that the OBWC was Petitioner's client, a determination which *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006) states, is a determination for the Court, not for the jury.

e. Limiting Instructions

Following the reading Petitioner's civil deposition testimony to the jury, the district court refused to give the proper limiting instruction specifically required in *United States v. Marvin Smith* 419 F. 3d 521 (6th Cir. 2005) that cautioned the jury not to place too much emphasis on the testimony or take it out of context. The district court only advised the jury not place too much emphasis on the testimony. The Sixth Circuit specifically requires a

two pronged caution, not the single prong given by the Court. The prejudice to Petitioner is palpable for the reason this instruction concerns the client-investor dichotomy. The district court's failure to give the two pronged instructions permitted the jury to take Petitioner's testimony out of context.

CONCLUSION

For the above reasons, the Court of Appeals should be reversed and Petitioner's conviction vacated.

November 23, 2010

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APPENDIX

SIXTH CIRCUIT COURT APPEALS FILINGS:

Order Denying Petition
for Rehearing,
filed 08/25/10 ..... A1 - A2

Opinion,
filed 07/14/10 ..... B1 - A27

NORTHERN DISTRICT OF OHIO FILINGS:

Judgment,
filed 12/31/08 ..... C1 - C14

OTHER:

Private Placement Memorandum
[*Excerpts*] ..... D1 - D46

No. 08-3892

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v.

MARK D. LAY,
Defendant-Appellant.

ORDER

BEFORE: GIBBONS, ROGERS, and KETHLEDGE, Circuit Judges.

The court having received a petition for rehearing en bane, which was circulated to all active judges of this court, none of whom requested a vote on the suggestion for rehearing en bane, the petition for rehearing has been referred to the original panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case.
Accordingly, the petition is denied.

ENTERED BY ORDER OF THE COURT
S/ Leonard Green
Leonard Green, Clerk

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v. No. 08-3892

MARK D. LAY,
Defendant-Appellant.

Appeal from the United States District Court
for the Northern District of Ohio at Cleveland.
No. 07-00339-001-David D. Dowd, District Judge.

Argued: April 27, 2010

Decided and Filed: July 14, 2010

Before: GIBBONS, ROGERS, and KETHLEDGE,
Circuit Judges.

COUNSEL

ARGUED: Michael L. Cioffi, BLANK ROME LLP, Cincinnati, Ohio, for Appellant. Antoinette T. Bacon, ASSISTANT UNITED STATES ATTORNEY, Cleveland, Ohio, for Appellee. **ON BRIEF**: Michael L. Cioffi, Nathaniel R. Jones, Rachel L. Payne, BLANK ROME LLP, Cincinnati, Ohio, for Appellant. Antoinette T. Bacon, Laura McMullen Ford, ASSISTANT UNITED STATES ATTORNEY, Cleveland, Ohio, for Appellee.

ROGERS, J., delivered the opinion of the court, in which GIBBONS, 1., joined. KETHLEDGE,J. (pp. 12-13), delivered a separate opinion concurring in part and dissenting in part.

OPINION

ROGERS, Circuit Judge. Defendant Mark D. Lay appeals his fraud convictions related to a hedge fund investment by the Ohio Bureau of Workers' Compensation. Lay primarily argues that the jury instructions were improper and that insufficient evidence supports the jury's verdict because, as a hedge fund adviser, Lay had a fiduciary relationship only with the hedge fund, not with its investors. Lay also seeks a new trial based on three of the district court's evidentiary rulings and its restitution and forfeiture determinations. Because a hedge fund adviser can, in some circumstances, have a fiduciary relationship with an investor, the jury instructions were correct and sufficient evidence supports Lay's conviction. We also reject Lay's challenges to the district court's evidentiary rulings and its restitution and forfeiture determinations.

I. Background

The facts of this case–based on the indictment and the evidence presented by the Government in support of the allegations in the indictment–are set out in careful detail in the district court's opinion denying Lay's motion for judgment of acquittal. *United States v. Lay*, 566 F. Supp. 2d 652,655-68 (N.D. Ohio 2008). A brief summary is sufficient here. In 1992 Lay began serving as investment adviser to the Ohio Bureau of Workers' Compensation when Lay's company, Capital Management, Inc., began managing the Bureau's investment in a long-term bonds fund, the Long Fund. The Bureau remained Lay's client as to its Long Fund investment from 1992 onward. In 1998, Lay founded the Active Duration Fund, a hedge fund. In September of 2003, the Bureau shifted $100 million from the Long Fund to the Active Duration Fund. The hedge fund agreement governing the Bureau's Active Duration Fund investment set a non-binding 150% leveraging guideline, but in fact Lay consistently leveraged Active Duration Fund assets far over 150%. In March of 2004, the Active Duration Fund lost $7 million. In May of 2004, after Bureau officials discussed the loss with Lay, the Bureau invested an additional $100

million in the Active Duration Fund. The Active Duration Fund's value continued to decline. In September of 2004, the Bureau invested an additional $25 million in that fund to avoid losing its entire investment, and then terminated its interest in the fund. The Bureau recovered only about $9 million from its $225 million Active Duration Fund investment.

A federal grand jury indicted Lay on one investment adviser fraud count and multiple mail and wire fraud counts. The investment adviser fraud count tracked the following Investment Advisers Act provisions, codified at 15 U. S. C. § 80b-6, which make it unlawful for an investment adviser to use the mails or the instrumentalities of interstate commerce

> (1) to employ any device, scheme, or artifice to defraud any client or prospective client;
> (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client;
> ....
> (4) to engage in any act, practice or course of business which is fraudulent, deceptive, or manipulative.

The Superseding Indictment charged that Lay acted to:

> (a) employ devices, schemes, and artifices to defraud, the client, the [Bureau] and thereby the [Active Duration Fund]; (b) engage in transactions, practices and courses of business which operated as a fraud and deceit upon, the client, the [Bureau] and thereby the [Active Duration Fund]; and (c) engage in any act, practice and course of business which was fraudulent, deceptive and manipulative, to wit: exercising leverage in excess of 150% in the [Active Duration Fund], in violation of the [hedge fund agreement], and concealing and failing to disclose to the full extent his exercise of leverage in excess of 150%.

The Superseding Indictment also alleged that Lay's conduct constituted mail fraud and wire fraud because Lay sent interstate emails, faxes, and trade confirmations to carry out these trades.

At trial, Terry Gasper, the Bureau's Chief Financial Officer and the person who initially decided to invest Bureau money in the Active Duration Fund, testified that his "understanding [of the Active Duration Fund and Long Fund investments] was that

if Mr. Lay felt that bond prices in general were going to decline. . . the [Active Duration Fund] would be used to hedge those bonds . . . so that if the bond market did, in fact, go down in value, we would make some money in the [Active Duration Fund] to offset the . . . unrealized losses we would have suffered in [the Long Fund]." Gasper indicated that his experience with Lay and the Long Fund was "one of the primary reasons" he invested in the Active Duration Fund, that he felt the Active Duration Fund investment was "very conservative" and "low risk," and that the Bureau was "simply diversifying the product under a current manager" when it invested Long Fund assets already under Lay's management in the Active Duration Fund. Gasper testified that in the first half of 2003, before the Bureau invested in the Active Duration Fund, Lay told Gasper that the Active Duration Fund "would be using leverage only to reflect the value of what he had in the fund" and that Gasper had viewed the 150% leveraging guideline in the hedge fund agreement as "a way to give [Lay] some flexibility in running money and moving monies around." Gasper testified that when the Bureau had invested a second $100 million in the Active Duration Fund, he had assumed that Lay was acting in "an appropriate fiduciary way . . . that the

leverage in the [Active Duration Fund] was exactly what we agreed to, that maximum of 150 percent of fund value."

James McLean, the Bureau's Chief Investment Officer, testified that he and Lay had agreed in April of 2004, after the initial $7 million loss and before the second $100 million investment, that "the fund was . . . intended to be more of a net positive rate of return fund . . . [meaning] that [Lay is] investing in high quality fixed income securities, and if they're yielding a rate of return of say five percent on an interest bearing basis, then that fund, all things being equal and nothing else being done, would earn a five percent rate of return." As to leverage, McLean testified that he and Lay agreed that the Active Duration Fund was "allowed to use a bit of leverage to take positions to enhance that five percent rate of return when [Lay saw] opportunities within the marketplace," but that with this "modest" leverage, "even if that account were to lose a little bit based upon the leveraging of a bet that [Lay] placed on the short position. . . you still earn one or two percent based upon the core of the hedge fund portfolio." Lay had regularly reported to McLean in writing regarding the Long Fund's performance, and these reports had included a one-line summary of the

Active Duration Fund's value under the heading "other assets."

FBI Special Agent Jeremy Durgin testified that, of the Bureau's $214 million total loss, approximately $212 million was due to trades that had leveraged Active Duration Fund assets over 150%. Durgin testified that Lay had begun leveraging those assets over 150% in early 2004, that two-thirds of Lay's Active Duration Fund trades involved leveraging over 150%, that over one-fifth of those trades involved leveraging over 1000%, and that some trades involved leveraging over 10,000%.

Over Lay's objection, the district court also permitted the jury to hear Lay's deposition testimony from a previous civil case. In that deposition, Lay repeatedly stated that his company, Capital Management, Inc., "was the investment adviser for the [Active Duration Fund]" and "provided a service to the [Active Duration Fund]." Lay also stated in that deposition that the Bureau was Capital Management, Inc.' s "client" and that "the Bureau, as a client, pays the fees."

The district court instructed the jury that, in order to find Lay guilty of investment adviser fraud, the Government had to prove "*each* element of *either* [15 U.S.C. §] 80b-6(1) *or* 80b-6(2) or 80b-6(4)." 566 F.

Supp. 2d at 692 (emphasis in original). With respect to §80b-6(1) & (2), the court instructed that

> In order to [establish that Lay committed investment adviser fraud under these provisions], the government must prove beyond a reasonable doubt that the [Bureau] was Mark Lay's client with respect to its investment in the. . . Active Duration Fund. . . .
>
> A client is an individual or entity which compensates an investment adviser to provide advice directly or through publications or writings about the value of securities or the advisability of investing in, purchasing, or selling securities. . . .
>
> It is for you to determine as a matter of fact whether Mark Lay had an investment adviser-client relationship with the [Bureau] with respect to its investment in the . . . Active Duration Fund. There are two possible outcomes of your determination on this issue.
>
> First, you could find that the government failed to prove beyond a reasonable doubt that Mark Lay had an investment adviser-client relationship with the [Bureau] with respect to its investment in the . . . Active Duration Fund.

> Second, you could find that the government [has] proved beyond a reasonable doubt that Mark Lay did have an investment adviser-client relationship with the [Bureau] with respect to the [Bureau's] investment in the. . . Active Duration Fund. You could make this finding in one of two ways. The Defendant does not dispute that he was the investment adviser and the [Bureau] was his client with respect to the Long Fund which continued throughout the period of time at issue in the Superseding Indictment. Therefore, you could find that: 1) Lay established a second investment adviser-client relationship with the [Bureau] and he was the investment adviser to the [Bureau] with respect to both the Long Fund and the. . . Active Duration Fund, or that 2) the investment adviser-relationship between Lay and the [Bureau] regarding the Long Fund was based on the investment of the monies in the Long Fund wherever it was invested and was not severed when Long Fund monies were invested in the ... Active Duration Fund.

Id. at 694-95.

The court also instructed with respect to § 80b-6(4) that if the jury found that the Bureau was not Lay's client with respect to the Active Duration Fund, the jury was to determine as a matter of fact whether Lay nonetheless had a fiduciary duty with regard to the Active Duration Fund. *Id.* at 696. The district court rejected Lay's objection to this instruction.

To find Lay guilty of mail or wire fraud, the district instructed the jury that it had to find beyond a reasonable doubt that (1) "there was a scheme to defraud;" (2) "[Lay] knowingly participated in the scheme;" (3) the scheme included a material representation or concealment of a material fact;" (4) "[Lay] had the intent to defraud;" and (5) "[Lay] used the mail or caused another to use the mail in furtherance of the scheme."

After deliberations began, the jury asked to rehear Lay's deposition testimony. The district court permitted a re-reading, but first cautioned the jury "not to accord undue influence to that testimony."

The jury found Lay guilty on all counts and found in a special verdict form that Lay had obtained $590,526.23 in proceeds from his mail and wire fraud offenses. Lay moved for judgment of acquittal and argued that insufficient evidence supported his

convictions because he did not owe the Bureau a fiduciary duty and the Bureau was not his client as to its Active Duration Fund investment. Lay also moved for a new trial based on, among other reasons, alleged error in the district court's jury instructions and its limiting instruction upon the re-reading of Lay's deposition testimony, and cumulative error.

The district court denied Lay's motion for judgment of acquittal. The court held that sufficient evidence supported the existence of a fiduciary relationship between Lay and the Bureau as to its Active Duration Fund investment because Lay had a pre-existing fiduciary relationship with the Bureau as to its Long Fund investment, the Bureau intended its Active Duration Fund investment to "provide Lay with flexibility and investment management alternatives for half of the [Long Fund] monies in order to reduce the overall risk to the [Bureau] monies under Lay's control," the Bureau was not a passive investor in the Active Duration Fund, the Bureau had "regular and direct" communication with Lay about the Active Duration Fund, and the Bureau was the sole shareholder in the Active Duration Fund. 566 F. Supp. 2d at 670-71. The district court denied Lay's motion for judgment of acquittal as to the mail and wire fraud counts. *Id.* at 671 n.56. The

district court also denied Lay's motion for a new trial and held that the jury instructions were proper, that the court had issued a proper limiting instruction before Lay's deposition testimony was re-read to the jury, and that no cumulative error had occurred. *Id.* at 672, 677-78, 678-79. The district court directed that $590,526.23 be forfeited and imposed $212 million in restitution. On appeal, Lay challenges the district court's jury instructions and its denial of his motions for judgment of acquittal and a new trial.

II. Jury-instruction and sufficiency-of-the-evidence challenges

A. Investment adviser fraud

Lay's central argument is that, as to the hedge fund, he owed no fiduciary duty to the Bureau. The duty of a hedge fund adviser, the theory goes, is to the hedge fund and cannot be to the various investors in the fund. If the theory is correct, then various instructions to the jury, permitting the jury to find such a fiduciary duty, were in error and, indeed, acquittal should have been ordered. The theory fails, however, for the reasons carefully stated by the district court below. *Id.* at 668-71. Permitting the jury to determine the existence of a fiduciary

relationship was proper and, on the facts of this case, a reasonable jury could find that Lay owed the Bureau a fiduciary duty with respect to the Active Duration Fund. Lay's challenges to the jury instructions and to the denial of the acquittal motion in this regard are therefore both without merit.

As explained by the district court, "there is evidence in the record that the characteristics of an adviser-client relationship were present between defendant and the [Bureau] regarding the [Active Duration Fund]." *Id.* at 670. Lay has never disputed that he had an investment adviser-client relationship–and therefore a fiduciary relationship–with the Bureau as to its Long Fund investment, and the evidence supports the conclusion that this relationship continued through the existence of the Active Duration Fund and encompassed the Bureau's Active Duration Fund investment. As Gasper testified, the Bureau invested in the Active Duration Fund to diversify existing investments, achieve positive returns regardless of market conditions, and increase returns above those the Bureau could achieve with the Long Fund alone. Capital Management, Inc.'s inclusion of the Active Duration Fund as "other assets" in its Long Fund reports indicates that the Active Duration Fund and

the Long Fund were part of a single investment strategy and therefore part of the Bureau's single relationship with Lay. Unlike a typical hedge fund investor, the Bureau was the only investor in the Active Duration Fund at the relevant time and the Bureau had an active role in its Active Duration Fund investment, as indicated by McLean's meetings with Lay regarding that investment. The jury could therefore reasonably find, as a matter of fact, that Lay owed the Bureau a fiduciary duty as to the Active Duration Fund investment.

Lay's categorical argument to the contrary is primarily based upon reading too much into the holding of the District of Columbia Circuit in *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006), regarding the Investment Advisers Act (IAA). That case precluded the Securities and Exchange Commission from treating all hedge fund investors as clients of a hedge fund adviser for purposes of circumventing a small-dealer registration exemption. The case did not hold that a hedge fund investor could never be a client of a hedge fund adviser, or be owed a fiduciary duty by one, for purposes of the criminal fraud provisions of the IAA.

In *Goldstein*, the D.C. Circuit considered an SEC rule change related to the IAA registration

exemption for investment advisers with fewer than fifteen clients in the past twelve months. *See id.* at 874. Under the SEC's prior rule, a hedge fund adviser's client for registration purposes was the fund, not the fund's investors. *Id.* at 876. Under the SEC's new rule, however, a hedge fund adviser's clients would include the fund's investors. *Id.* at 877. The court held that the SEC had not "adequately explained how the relationship between hedge fund investors and advisers justifies treating the former as clients of the latter" and vacated the new rule. *Id.* at 882. The court reasoned that, based on the IAA's definition of "investment adviser," a client relationship results when the investor receives investment advice directly from the adviser, and because hedge fund investors do not always receive direct investment advice from hedge fund advisers, the IAA does not support treating all hedge fund investors as clients of hedge fund advisers. *Id.* at 879. As the court stated, "[a hedge fund adviser] does not tell the *investor* how to spend his money; the investor made that decision when he invested in the [hedge] fund. Having bought into the fund, the investor fades into the background; his role is completely passive." *Id.* at 879-80.

Goldstein did not hold that no hedge fund adviser could create a client relationship with an investor, but rather held only that the SEC had "not justified treating *all* investors in hedge funds as clients." *Id.* at 883. The court noted that hedge funds are "usually structured as limited partnerships to achieve maximum separation between ownership and management" and that "the general partner manages the fund . . . for a fixed fee and a percentage of the gross profits from the fund" while "[t]he limited partners are passive investors and generally take no part in management activities." *Id.* at 876. The court acknowledged that "different classes of investors [may] have different rights or privileges with respect to their investments" and that "[i]f . . . certain characteristics present in some investor-adviser relationships. . . mark a 'client' relationship, then the [SEC] should have identified those characteristics and tailored its rule accordingly." *Id.* at 882-83. It was therefore entirely consistent with *Goldstein* for the district court in Lay's case to permit the jury to find as fact that Lay owed the Bureau a fiduciary duty with respect to the Active Duration Fund. The jury's finding that Lay was guilty of investment adviser fraud is also consistent with *Goldstein* because the relationship between the Bureau and

Lay as to the Active Duration Fund was not a typical hedge fund adviser-investor relationship.

This disposes of the bulk of Lay's arguments on appeal. Lay also argues that the 150% limit on leveraging served only as a guideline rather than a binding limitation. However, the leeway contemplated by the leveraging guideline's non-binding nature does not permit leveraging over 150% in two-thirds of trades and leveraging over 1,000% in one-fifth of trades. Therefore, the district court's jury instructions fairly and adequately submitted the issues and applicable law to the jury, *United States v. Mick*, 263 F.3d 553, 569 (6th Cir. 2001) (standard), and, viewing the evidence in the light most favorable to the Government, a rational trier of fact could have found Lay guilty of investment adviser fraud based on his misrepresentation of or failure to disclose his leveraging activity to his client, the Bureau, *Jackson v. Virginia*, 443 U.S. 307, 319 (1979) (standard).

B. Mail and wire fraud

Sufficient evidence also supports the jury's determination that Lay is guilty of mail and wire fraud. The evidence establishes that Lay used

interstate mail or wires in furtherance of a scheme or artifice to defraud with intent to deprive the Bureau of money when he misrepresented to the Bureau the extent of his overleveraging and omitted material information in his reports to the Bureau. *See United States v. Prince*, 214 F.3d 740, 747-48 (6th Cir. 2000) (elements of the offense). When Gasper invested Bureau money in the Active Duration Fund, he believed the investment was conservative because Lay had represented that he would leverage based on the 150% guideline, and Gasper increased the Bureau's Active Duration Fund investment based on the same belief; therefore, Lay's misrepresentations of his leveraging activity caused the Bureau to part with money. The trade confirmations, emails, and faxes through which Lay conducted the fraud satisfy the mailing and wiring requirements because these documents "were designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Daniel*, 329 F.3d 480, 489 (6th Cir. 2003). Therefore, viewing the evidence in the light most favorable to the Govermnent, a rational trier of fact could have found Lay guilty of mail and wire fraud.

Moreover, the district court's jury instructions on mail and wire fraud were also proper, and–for the reasons set out above with regard to the IAA–the district court properly declined to instruct the jury that, as a matter of law, Lay owed the Bureau no fiduciary duty and that Lay therefore could not be convicted of mail and wire fraud.

III. New trial motion

Lay is not entitled to a new trial because the three challenged evidentiary rulings were correct, the district court correctly determined restitution and forfeiture, and no cumulative error occurred.

The record belies Lay's contention that the Government consistently called the Bureau Lay's "client" at trial or interchanged the words "investor" and "client." Lay's own counsel, during cross-examination of a Bureau official, solicited the most significant discussion of this nature. Lay cannot complain about the discussion elicited by his own counsel, and other isolated references to the Bureau as Lay's client as to its Active Duration Fund investment do not warrant a new trial.

Lay's deposition testimony from a previous case was admissible non-hearsay because it is an

admission by a party-opponent, Fed. R. Evid. 801(d)(2); *see United States v. Moffie*, 239 F. App'x 150, 156-57 (6th Cir. 2007), and the deposition was not rendered inadmissible because Lay opined therein that the Bureau was his client. A lay witness may testifY to a legal conclusion that "does not involve terms with a separate, distinct and specialized meaning in the law different from that present in the vernacular." *United States v. Sheffiy*, 57 F.3d 1419, 1426 (6th ir. 1995). Because "client" does not have a separate, distinct, and specialized meaning in the law different from its meaning in the vernacular, the district court correctly permitted the jury to hear Lay's deposition and Lay was not entitled to a new trial on this basis.

Before permitting the re-reading of Lay's deposition testimony, the district court properly cautioned the jury "not to accord undue influence to that testimony." Lay's additional requested instruction, that the jury was not to take the testimony out of context, was unnecessary because the entirety of Lay's deposition testimony was re-read to the jury. In *United States v. Epley*, 52 F.3d 571, 579 (6th Cir. 1995), we ruled that a district court had not abused its discretion in re-reading testimony to a jury, reasoning in part that the danger of the jury's

taking the testimony out of context was not present because the jury re-heard the entire testimony of the witness. Therefore Lay was not entitled to a new trial based on the district court's refusal to instruct the jury not to take the re-read deposition testimony out of context.

The district court correctly ordered that $590,526.23 be forfeited based on the amount the jury found to represent or to be traceable to proceeds that Lay obtained from his mail and wire fraud. *See* 18 U.S.C. §§ 981, 982. The district court also properly imposed $212 million in restitution because this amount reflects the Bureau's losses due to Lay's over-leveraging of Active Duration Fund assets. As we held in *United States v. Sosebee*, 419 F.3d 451, 461 (6th Cir. 2005), such "restitution orders are not affected by the Supreme Court's ruling in *Apprendi v. New Jersey*, 530 U.S. 466 (2000), because the restitution statutes do not specify a statutory maximum." Therefore, Lay was not entitled to a new trial on this basis.

Finally, because Lay's individual claims of error fail, Lay was not entitled to a new trial based on cumulative error.

IV. Conclusion

For the foregoing reasons, the judgment of the district court is affirmed.

CONCURRING IN PART, DISSENTING IN PART

KETHLEDGE, Circuit Judge, concurring in part and dissenting in part. I join all but part II.B of the court's opinion. I dissent from that part because I do not think the government proved a case of mail fraud.

That is not to say it could not have. The government had ample proof that Lay defrauded the Bureau by misrepresenting his intentions with respect to the 150% leverage limitation, and that he did so in order to induce the Bureau to part with its money. The only remaining element of mail fraud was an interstate mailing "in furtherance of the scheme[.]" *United States v. Prince*, 214 F.3d 740, 748 (6th Cir. 2000); *see also* 18 U.S.C. § 1341 (a mailing must be "for the purpose of executing such scheme or artifice" to defraud). Given the abundance of proof as to Lay's misrepresentations generally, one might expect simply to see proof that one of them was mailed.

But we do not see that. Instead, the charged mailings are "trade confirmation slips," which one bank mailed to another as a result of trades that Lay authorized for the Active Duration Fund. No one

contends that the slips themselves contained any misrepresentations or that they played any role whatever in parting the Bureau from its money. Instead, the slips simply confirmed trades that Lay had made on the open market. The question, then, is whether the government proved the slips somehow furthered the fraud.

The government's explanation of this point is amorphous at best. It observes, correctly, that post-fraud mailings can further the scheme if "designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Lane*, 474 U.S. 438, 451 (1986) (internal quotation marks omitted); *see also* Majority Op. at 10. The government contends the slips had this effect because they ensured that the Fund would not be assessed a five-percent penalty for failed trades. Had those penalties been assessed, the government says, Lay would have "lost [the Bureau's] confidence and business." Gov't Br. at 52. The government's explanation more or less trails off there; but we are left to infer, apparently, that had the Bureau lost confidence in Lay, it would have begun asking questions, whose answers might have

led to still other questions, which in turn could have uncovered the fraud. So, in the government's view, the slips furthered the scheme.

The question is one of degree. In my view, the bank slips were too remote from the antecedent fraud, and too speculative in their effects, to support a finding that they were "designed to lull the victims into a false sense of security[.]" *Lane*, 474 U.S. at 451. If the slips here were so designed, so too were Lay's annual submissions to the SEC to retain his status as a registered investment advisor, *see* 17 C.F.R. § 275.204-1; since absent that status the Bureau surely would have lost confidence in him. That is an awfully broad conception of mailings in furtherance of the fraudulent scheme. At some point the element exists only in theory, rather than in fact.

That said, I agree with the majority's affirmance of Lay's conviction for conspiracy to commit mail fraud and wire fraud. On that charge, the government did identify an overt act that concealed the fraudulent scheme from the Bureau. And my agreement on the conspiracy charge means that, even under my proposed disposition of this case, Lay's sentence would remain the same. The district court sentenced Lay to 60 months for the investment-adviser conviction, and 144 months for

each of the other convictions–including the conspiracy one–with all sentences running concurrently. Even absent the mail-fraud convictions, therefore, Lay's sentence would be 144 months. Thus, while I respectfully dissent from the majority's affirmance of Lay' s mail-fraud convictions, I join its affirmance of his sentence.

But my point, in closing, remains a practical one: The government would make its task easier in mail- and wire-fraud cases ifit would choose, as its charged communication, a blood relative of the fraud, rather than a second cousin by marriage. Reasonable jurists can disagree as to the outcome in cases like this one. But one wonders why they should have to.

For these reasons, I concur in part and dissent in part.

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 08-3892

UNITED STATES OF AMERICA,
Plaintiff - Appellee,

v.

MARK D. LAY,
Defendant - Appellant.

Before: GIBBONS, ROGERS, and KETHLEDGE, Circuit Judges.

JUDGMENT

On Appeal from the United States District Court for the Northern District of Ohio at Cleveland.

THIS CAUSE was heard on the record from the district court and was argued by counsel.

IN CONSIDERATION WHEREOF, it is ORDERED that the judgment of the district court is AFFIRMED.

ENTERED BY ORDER OF THE COURT
S/ Leonard Green
Leonard Green, Clerk

United States District Court
Northern District of Ohio

UNITED STATES OF AMERICA

v.

Mark D. Lay

Case Number:
1:07CR00339-001

USM Number:
55409-060

Richard M. Kerger and
Percy Squire
Defendant's Attorney

***AMENDED**
(to correct restitution amount)
JUDGMENT IN A CRIMINAL CASE

THE DEFENDANT:

X was found guilty on count(s) 1 and 4 of the Superseding Indictment after a plea of not guilty.

The defendant is adjudicated guilty of these offense(s):

Title & Section	Nature of Offense	Offense Ended	Count
15 USC Section 80b-6 & 80b-17	Investment Advisory Fraud	January 2005	1
18 USC Section 1349	Conspiracy to Commit or Attempt Mail & Wire Fraud	January 2005	2
18 USC Section 1341 & 2	Mail Fraud, Aiding & Abetting	January 2005	3 & 4

The defendant is sentenced as provided in pages 2 through 6 of this judgment. The sentence is imposed pursuant to the Sentencing Reform Act of 1984.

IT IS ORDERED that the defendant shall notify the United States Attorney for this district within 30 days of any change of name, residence, or mailing address until all fines, restitution, costs, and special assessments imposed by this judgment are fully paid. If ordered to pay restitution, the defendant must notify the court and the United

States Attorney of material changes in the defendant's economic circumstances.

July 8, 2008
Date of Imposition of Judgment

s/ David D. Dowd, Jr.
Signature of Judicial Officer

DAVID D. DOWD. JR.,
United States Senior District Judge
Name & Title of Judicial Officer

July 11, 2008
Date

IMPRISONMENT

The defendant is hereby committed to the custody of the United States Bureau of Prisons to be imprisoned for a term of 60 months as to Count 1 and 144 Months as to each of Counts 2, 3 and 4, and all counts to run concurrently with each other.

[X] The defendant is remanded to the custody of the United States Marshal.

RETURN

I have executed this judgment as follows:

_____

_____

Defendant delivered on _____ to _____

_____ at _____ with a certified copy of this judgment.

_____

UNITED STATES MARSHAL

By _____

Deputy U.S. Marshal

SUPERVISED RELEASE

Upon release from imprisonment, the defendant shall be on supervised release for a term of 3 Years.

The defendant must report to the probation office in the district to which the defendant is released within 72 hours of release from the custody of the Bureau of Prisons.

The defendant shall not commit another federal, state, or local crime.

The defendant shall not unlawfully possess a controlled substance. The defendant shall refrain from any unlawful use of a controlled substance. The defendant shall submit to one drug test within 15 days of release from imprisonment and at least two periodic drug tests thereafter, as determined by the Court.

[] The above drug testing condition is suspended, based on the court's determination that the defendant poses a low risk of future substance abuse. (Check, if applicable.)

[] The defendant shall not possess a firearm, ammunition, destructive device, or any other dangerous weapon. (Check, if applicable.)

[X] The defendant shall cooperate in the collection of DNA as directed by the probation officer. (Check, if

applicable.)

[] The defendant shall register with the state sex offender registration agency in the state where the defendant resides, works, or is a student, as directed by the probation officer. (Check, if applicable.)

[] The defendant shall participate in an approved program for domestic violence. (Check, if applicable.)

If this judgment imposes a fine or restitution, it is a condition of supervised release that the defendant pay in accordance with the Schedule of Payments sheet of this judgment.

The defendant must comply with the standard conditions that have been adopted by this court as well as with any additional conditions on the attached page.

STANDARD CONDITIONS OF SUPERVISION

1) the defendant shall not leave the judicial district without the permission of the court or probation officer;
2) the defendant shall report to the probation officer and shall submit a truthful and complete written report within the first five days of each month;
3) the defendant shall answer truthfully all inquiries by the probation officer and follow the instructions of the probation officer;

4) the defendant shall support his or her dependents and meet other family responsibilities;

5) the defendant shall work regularly at a lawful occupation, unless excused by the probation officer for schooling, training, or other acceptable reasons;

6) the defendant shall notify the probation officer at least ten days prior to any change in residence or employment;

7) the defendant shall refrain from excessive use of alcohol and shall not purchase, possess, use, distribute, or administer any controlled substance or any paraphernalia related to any controlled substances, except as prescribed by a physician;

8) the defendant shall not frequent places where controlled substances are illegally sold, used, distributed, or administered;

9) the defendant shall not associate with any persons engaged in criminal activity and shall not associate with any person convicted of a felony, unless granted permission to do so by the probation officer;

10) the defendant shall permit a probation officer to visit him or her at any time at home or elsewhere and shall permit confiscation of any contraband observed in plain view of the probation officer;

11) the defendant shall notify the probation officer within seventy-two hours of being arrested or questioned by a law enforcement officer;

12) the defendant shall not enter into any

agreement to act as an informer or a special agent of a law enforcement agency without the permission of the court; and

13) as directed by the probation officer, the defendant shall notify third parties of risks that may be occasioned by the defendant's criminal record or personal history or characteristics and shall permit the probation officer to make such notifications and to confirm the defendant's compliance with such notification requirement.

SPECIAL CONDITIONS OF SUPERVISED

The defendant shall provide the probation officer access to all requested financial information.

The defendant shall not incur new credit charges or open additional lines of credit without the approval of the probation officer.

The defendant shall apply all monies received from income tax refunds, lottery winnings, judgments, and/or other anticipated or unexpected financial gains to the outstanding court-ordered financial obligation.

The defendant is ordered to forfeit to the United States the sum of $590,526.23.

CRIMINAL MONETARY PENALTIES

The defendant must pay the total criminal monetary penalties under the Schedule of Payments on Sheet 6.

	Assessment	Fine	Restitution
TOTALS	$400.00	$0.00	$212,967,084.76

_____ The determination of restitution is deferred until ___. An Amended Judgment in a Criminal Case (AO 245C) will be entered after such determination.

_____ The defendant must make restitution (including community restitution) to the following payees in the amount listed below.

If the defendant makes a partial payment, each payee shall receive an approximately proportioned payment, unless specified otherwise in the priority order or percentage payment column below. However, pursuant to 18 U.S.C. § 3664(I), all nonfederal victims must be paid before the United States is paid.

Name of Payee	Total Loss*	Restitution Ordered	Priority of Percentage

Ohio Bureau of
Worker's Compensation
30 West Spring Street L-24
Columbus, OH 43215
Attention: Tracy L. Valentino,
Chief Fiscal & Planning Officer

TOTALS * $22,967,084.76

_____ Restitution amount ordered pursuant to plea agreement $ _____

_____ The defendant must pay interest on restitution and a fine of more than $2,500, unless the restitution or fine is paid in full before the fifteenth day after the date of the judgment, pursuant to 18 U.S.C. § 3612(f). All of the payment options on the Schedule of Payments sheet may be subject to penalties for delinquency and default, pursuant to 18 U.S.C. § 3612(g).

_____ The court determined that the defendant does not have the ability to pay interest and it is ordered that:

____ the interest requirement is waived for the _____ fine _____ restitution.

____ the interest requirement for the ____ fine ____ restitution is modified as follows:

*Findings for the total amount of losses are required under Chapters 109A, 110, 110A, and 113A of Title 18 for offenses committed on or after September 13, 1994, but before April 23, 1996.

SCHEDULE OF PAYMENTS

Having assessed the defendants ability to pay, payment of the total criminal monetary penalties are due as follows:

A [] Lump sum payment of $_____ due immediately, balance due

[] not later than _____ or
[] in accordance [] C, [] D, [] E, or [] F below; or

B [X] Payment to begin immediately (may be combined with [] C, [] D, [] E, or [X] F below; or

C [] Payment in equal installments of $___ over a period of __ , to commence __ days after the date of this judgment; or

D [X] The defendant shall pay 25% of defendant's gross income per month, through the Federal Bureau of Prisons Inmate Financial Responsibility Program. If a restitution balance remains upon release from imprisonment, payment is to commence no later than 60 days following release from imprisonment to a term of supervised release in equal monthly payments, or a least a minimum of 20% of defendant's gross monthly income during the term of supervised release and thereafter as prescribed by law. Notwithstanding establishment of a payment

schedule, nothing shall prohibit the United States from executing or levying upon property of the defendant discovered before and after the date of this Judgment.

E [] Payment during the term of supervised release will commence within _ (e.g., 30 or 60 days) after release from imprisonment. The court will set the payment plan based on an assessment of the defendant's ability to pay at that time; or

F [X] Special instructions regarding the payment of criminal monetary penalties:

[X] A special assessment of $400.00 is due in full immediately as to count(s) 1 through 4. PAYMENT IS TO BE MADE PAYABLE AND SENT TO THE CLERK, U.S. DISTRICT COURT

[] After the defendant is release from imprisonment, and within 30 days of the commencement of the term of supervised release, the probation officer shall recommend a revised payment schedule to the Court to satisfy any unpaid balance of the restitution. The Court will enter an order establishing a schedule of payment.

Unless the court has expressly ordered otherwise, if this judgment imposes imprisonment, payment of criminal monetary penalties is due during

imprisonment. All criminal monetary penalties, except those payments made through the Federal Bureau of Prisons' Inmate Financial Responsibility Program, are made to the clerk of the court.

The defendant shall receive credit for all payments previously made toward any criminal monetary penalties imposed.

[] Joint and Several (Defendant names, Case Numbers, Total Amount, Joint and Several Amount, and corresponding payee.)

[] The defendant shall pay the cost of prosecution.

[] The defendant shall pay the following court cost(s):

[] The defendant shall forfeit the defendant's interest in the following property to the United States:

Payments shall be applied in the following order: (1) assessment, (2) restitution principal, (3) restitution interest, (4) fine principal, (5) fine interest, (6) community restitution, (7) penalties, and (8) costs, including the cost of prosecution and court costs.

Copy No.: _____
Issued to: _____

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

MDL ACTIVE DURATION FUND, LTD.

(An exempted mutual fund company incorporated with limited liability under the laws of Bermuda)
Offering of Non-Voting, Redeemable, Participating Shares
Minimum Subscription Per Investor: U.S. $1,000,000
MDL CAPITAL MANAGEMENT, INC.
Investment Adviser
OLYMPIA CAPITAL INTERNATIONAL, INC.
Administrator

THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER APPLICABLE LAW AND UNDER THE PROVISIONS OF THE FUND'S GOVERNING DOCUMENTS.

THE DATE OF THIS MEMORANDUM IS SEPTEMBER 22, 2003

LEGENDS

PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO

THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE RESTRICTIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY DOUBT ABOUT THE CONTENTS OF THIS MEMORANDUM, YOU SHOULD CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

NEITHER MDL ACTIVE DURATION FUND, LTD. (THE "FUND") NOR THE PARTICIPATING SHARES OF THE FUND (THE "SHARES") DESCRIBED IN THIS MEMORANDUM (THIS "MEMORANDUM") HAVE BEEN OR WILL BE REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF THE UNITED STATES ("U.S.") OR ANY OTHER JURISDICTION. THIS MEMORANDUM SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY, NOR SHALL THERE BE ANY SALE OF SHARES IN ANY JURISDICTION IN WHICH SUCH OFFER, SOLICITATION OR SALE IS NOT AUTHORIZED OR TO ANY PERSON TO WHOM IT IS UNLAWFUL TO MAKE SUCH OFFER, SOLICITATION OR SALE. THE DIRECT OR INDIRECT OWNERSHIP OF SHARES BY "RESTRICTED PERSONS" AS DEFINED IN THIS MEMORANDUM IS PROHIBITED. NO PERSON HAS BEEN AUTHORIZED TO MAKE ANY REPRESENTATIONS CONCERNING THE FUND OR THE SHARES WHICH ARE INCONSISTENT

WITH THOSE CONTAINED IN THIS MEMORANDUM, AND ANY SUCH REPRESENTATIONS SHOULD ACCORDINGLY BE TREATED AS UNAUTHORIZED AND MAY NOT BE RELIED WON BY THE RECIPIENT.

UPON THE INVESTMENT ADVISER'S REGISTRATION WITH THE UNITED STATES COMMODITY FUTURES TRADING COMMISSION, THIS FUND WILL TRADE IN FUTURES. PURSUANT TO AN EXEMPTION FROM THE COMMODITY FUTURES TRADING COMMISSION IN CONNECTION WITH POOLS WHOSE PARTICIPANTS ARE LIMITED TO QUALIFIED ELIGIBLE PARTICIPANTS, A CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM FOR THIS POOL IS NOT REQUIRED TO BE, AND HAS NOT BEEN, FILED WITH THE COMMISSION. THE COMMODITY FUTURES TRADING COMMISSION DOES NOT PASS WON THE MERITS OF PARTICIPATING IN A POOL OR WON THE ADEQUACY OR ACCURACY OF A CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM. CONSEQUENTLY, THE COMMODITY FUTURES TRADING COMMISSION HAS NOT REVIEWED OR APPROVED AND IS NOT EXPECTED TO REVIEW OR APPROVE THIS CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM.

CERTAIN TRANSACTIONS IN FINANCIAL FUTURES AND RELATED OPTIONS AND THE INVESTMENT AND/OR HEDGING STRATEGIES ASSOCIATED THEREWITH WILL NOT BE AVAILABLE TO THE FUND UNLESS AND UNTIL

CERTAIN REGISTRATIONS ARE OBTAINED. THE INVESTMENT ADVISER IS SUBMITTING APPLICATIONS FOR SUCH REGISTRATIONS BUT IS NOT OBLIGATED TO PURSUE OR OBTAIN ANY SUCH REGISTRATIONS.

THE PURCHASE OF SHARES IS SPECULATIVE AND INVOLVES A HIGH DEGREE OF RISK. THERE IS NO ASSURANCE THAT THE FUND WILL BE PROFITABLE. SEE THE SECTION ENTITLED "RISK FACTORS" WITHIN THIS MEMORANDUM FOR A DESCRIPTION OF CERTAIN RISKS INVOLVED IN THE PURCHASE OF SHARES.

THIS MEMORANDUM IS INTENDED SOLELY FOR THE USE OF THE PERSON TO WHOM IT HAS BEEN DELIVERED BY THE FUND FOR THE PURPOSE OF EVALUATING A POSSIBLE INVESTMENT BY THE RECIPIENT IN THE SHARES DESCRIBED HEREIN, AND IT IS NOT TO BE REPRODUCED OR DISTRIBUTED TO ANY OTHER PERSONS (OTHER THAN PROFESSIONAL ADVISERS OF THE PROSPECTIVE INVESTOR RECEIVING

THIS DOCUMENT FROM THE FUND). THIS DOES NOT CONSTITUTE AN OFFERING TO ANY MEMBER OF THE GENERAL PUBLIC OF BERMUDA.

All monetary amounts for Shares set forth herein are expressed in U.S. dollars.

INTRODUCTION

MDL Active Duration Fund, Ltd. (the "Company" or the "Fund"), is an exempted, open ended mutual fund company incorporated under Bermuda law with limited liability and with unlimited duration. The Fund has been formed specifically for the purpose of providing an investment vehicle through which United States tax-exempt institutional investors and non-U.S. persons ("Investors") can invest in a portfolio consisting primarily of U.S. Treasury notes and bonds, U.S. agency notes and bonds and corporate and mortgage-backed fixed income securities. The Fund's duration, maturity structure and overall quality rating will be adjusted periodically based on an assessment of certain macro-economic factors. The Fund will seek to capture significant gains during periods when interest rates are generally declining and will seek to protect principal during periods when rates are generally rising.

The Fund's investment adviser is MDL Capital Management, Inc., a Pennsylvania corporation ("MDL" or the "Investment Adviser"). The Investment Adviser will provide investment advisory services to the Fund and will be responsible for the overall management of the Fund's portfolio. The Investment Adviser is a registered as an investment adviser with the U.S. Securities and Exchange Commission (the "SEC") under the Investment Advisers Act of 1940 (the "Advisers Act"). The Fund's investment objective is to profit by investing in U.S. Treasury, U.S. government agency, corporate and

mortgage-backed fixed income securities, currencies, short-term equity positions, futures and option contracts.

The Fund's investment strategy will include the use of leverage. ***The Investment Adviser, in its sole and absolute discretion and authority as investment advisor to the Fund will ultimately identify and select investments for the Fund.*** The Fund is designed primarily for U.S. tax-exempt institutional Investors and non-U.S Investors. There can be no assurance that the Fund will achieve its objectives.

The Fund is offering (the "Offering") its non-voting, redeemable, participating shares (the "Shares"), subject to prior subscription and other conditions. The Fund has a target equity capitalization of $300 million (which may be increased or decreased in the discretion of the board of directors of the Company (the "Board of Directors")). The minimum initial subscription per Investor is U.S. $1,000,000, subject to reduction in the discretion of the Board of Directors of the Company. Initially, Shares will be offered at U.S. $1,000.00 per Share. After commencement of investing activities, Shares will be offered for sale at the Net Asset Value per share as of the close of business on the last business day of each quarter (and any other date approved by the Board of Directors). The Shares are offered only to non-United States persons and certain U.S. tax-exempt Investors which meet the definitions of "qualified purchaser" as defined in the Investment Company Act of 1940, as amended (the "Investment Company Act") and

Qualified Eligible Purchaser as defined in Regulation 4.7 of the Commodity Futures Trading Commission. The Fund reserves the right to reject any subscription in whole or in part.

The initial offering period shall commence on the earlier of the date of the publication of this Memorandum, and the date of the filing of this Memorandum with the Registrar of Companies in Bermuda on September 22, 2003 (the "Initial Offering Period") and will end on the earlier to occur of the acceptance of subscriptions in the aggregate amount of $3,000,000 or January 12, 2004 (the "Initial Closing Date").

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SUMMARY
SUMMARY OF THE TERMS OF THE OFFERING AND THE FUND

The following is a summary of certain information about the Fund and the offering of Shares made by means of this Confidential Private Placement Memorandum (the "Memorandum"). The summary is qualified in its entirety by the more complete information appearing elsewhere in the Memorandum, and is subject to the detailed provisions of the Fund's Governing Documents and the Subscription Agreement attached hereto as Exhibit A. The Offering is subject to prior sale, modification and withdrawal.

FUND OVERVIEW

The Fund

The Fund is a Bermuda exempted, open ended mutual fund company incorporated on May 20, 2002 with limited liability in Bermuda. The operation and management of the Fund are governed by its Memorandum of Association and Bye-Laws, copies of which are available from the Administrator (the "Governing Documents"). The Registered Office and principal place of business of the Fund is Williams House, 20 Reid Street, Hamilton, HM11, Bermuda. The Fund has been classified as a Bermuda Institutional Scheme under the Bermuda Monetary Authority Collective Investment Scheme Regulations of 1998, as amended (the "Regulations"), and will be subject to the provisions of such law.

Investment Adviser

The Investment Adviser of the Fund is MDL Capital Management, Inc., a Pennsylvania corporation. The Investment Adviser's principal shareholders are Mark D. Lay, Steven L. Sanders, Edward Adatepe and Safeguard Scientific, Inc. The Investment Adviser is registered with the U.S. Securities and Exchange Commission as an investment adviser. The Investment Adviser is registering to become licensed as a commodity pool operator ("CPO") with the Commodity Futures Trading Commission ("CFTC"). Upon receipt of such licenses, the Investment Adviser will be the pool operator of the Fund.

Board of Directors

The Fund is governed by its board of directors (the "Directors" or "Board of Directors"). The members of the Board of Directors are Mark D. Lay, Steven L. Sanders and Edward Adatepe, who are the principals of the Investment Adviser, and Oskar P. Lewnowski and Raymond Morrison of Olympia Capital International, Inc., the Fund's administrator.

The Master Fund

The Fund may at some point in the future choose to invest all or some portion of its assets in a centralized investment company, commonly known as a "master fund" (the "Master Fund") (the Fund being a "feeder fund"). Such an investment would also be managed by the Investment Adviser at that level, but at all times in accordance with the investment style and strategies of the Fund as described in this Memorandum. The Master Fund would be a

Bermuda limited liability entity or State of Delaware limited partnership or similar entity eligible to be treated as a "partnership" for U.S. income tax purposes. It is anticipated that the Master Fund, if established, would admit one or more additional Investor Members consisting of other investment funds organized by the Investment Adviser to participate in the portfolio of the Master Fund.

Investment Objectives

The investment objectives of the Fund shall be to concentrate on investments in U.S. Treasury notes and bonds, U.S. government agency notes and bonds and corporate and mortgage-backed fixed income securities to generate consistent positive returns and to achieve an investment return in excess of that from the investment grade, broad market debt securities reflected in the Lehman Brothers Government Credit Bond Index (the "Lehman Government Credit Index"). In particular, the Fund will seek to significantly outperform the Index during periods when interest rates are generally declining and will seek to protect principal during periods when rates are generally rising. The Fund will seek to meet these objectives through an "active duration" approach, *e.g.*, the Fund's portfolio will be constructed to take advantage of anticipated movements in yield curves as well as inter - sector spread relationships. The variation in the Fund's average duration will be based upon the Investment Adviser's projections as to overall trends in these variables based on analysis of U.S. and global macro-economic growth factors. The Fund's portfolio will

include publicly-traded, United States-issued government agency, corporate and mortgage-backed fixed income securities and U.S. money market instruments and short-term investment funds, guaranteed investment contracts, forward contracts and, following the Investment Adviser's registration as a CPO with the CFTC, interest rate futures, financial futures and options thereon. The investments of the Fund will also involve the purchase of long and short positions of equity and investments and positions in foreign currencies. It is anticipated that the assets of the Fund will sometimes be pledged or otherwise collateralized to obtain a certain degree of leverage. The investments will be selected by the Investment Adviser in a manner consistent with the investment return objectives established by the Investment Adviser from time to time consistent with prudent standards of diversification, liquidity, quality, volatility and portfolio turnover. There is no assurance that the Fund will achieve its objectives.

Administrator

Olympia Capital International, Inc. (the "Administrator"), a British Virgin Islands corporation with a managing office in Bermuda, serves as administrator to the Fund. The Administrator will provide various administrative services to the Fund, including the calculation of the Fund's Net Asset Value and Net Asset Value per Share, processing Share subscriptions and redemptions and maintaining the Fund's principal books and records.

Registrar and Transfer Agent
The Fund has appointed Winchester Fiduciary Services Limited, located in Hamilton, Bermuda, as registrar and transfer agent (the "Registrar and Transfer Agent"). The Registrar and Transfer Agent is wholly-owned by Winchester Global Trust Company Limited, an affiliate of the Administrator.

Custodian
The Fund has engaged Credit Suisse First Boston Corporation, a Massachusetts corporation, to serve as custodian of the Fund's assets (the "Custodian"). The Custodian will also act as the prime broker of the Fund.

Potential Advantages of the Fund
The Fund is designed to enable Investors to access investment and trading strategies that are not generally available to most investors; to participate in investment programs that differ from those of traditional portfolio management; to diversify their investment portfolios; and to benefit from the investment techniques and strategies of the Investment Adviser.

Leverage
The Fund is expected to leverage the Fund's investment portfolio as a means to increase yield and enhance total return. Up to 150% of the Fund's assets, at the time of investment, may be leveraged (*i.e.*, the combined value of borrowings and short positions). Leveraging will include, but is not limited to, short selling of securities, reverse repurchase

agreements, certain option and futures transactions plus any borrowings to leverage the Fund's assets. Although the use of leverage may enhance returns on the Fund's portfolio and increase the number of investments that may be made by the Fund, it may also substantially increase the risk of loss. The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.

THE OFFERING

The Shares

The Fund is offering up to 10,000,000 non-voting, redeemable participating shares, U.S. $0.001 par value (the "Shares"). The Fund's share capital consists of the Shares and 100 voting, non-participating, non-redeemable shares, U.S. $0.01 par value each (the "Management Shares"), which are held by the MDL Active Duration Purpose Trust, a trust formed under the laws of Bermuda (the "Purpose Trust"). Harrington Trust Limited, a Bermuda company, is the sole trustee of the Purpose Trust. See "MANAGEMENT AND ADMINISTRATION--The Purpose Trust."

Plan of Distribution

The Fund intends to sell Shares which will be denominated in U.S. Dollars. Each Share will be issued at a price of U.S. $1,000.00 during the Initial Offering Period. There is no assurance that the Fund will receive and accept the minimum aggregate subscription amount necessary to commence

investing. If subscriptions totaling at least $3,000,000 are not accepted by the Fund during the Initial Offering Period, the subscriptions will be returned with interest actually earned thereon.

Continuous Offering Period

If at least $3,000,000 in subscriptions are accepted, the Fund will commence investing operations. Subsequent to the Initial Offering Period, Shares will be offered at the Net Asset Value per Share as of the last Business Day of each calendar quarter (each, a "Valuation Date"). Shares purchased after the Initial Offer Period will be issued as of the next Business Day after the relevant Valuation Date (the "Subscription Date"). A Business Day shall mean a day on which banks are open for business in Bermuda and New York, other than a Saturday or Sunday. Such proceeds will be invested in the Fund for the benefit of the Investor at the next Investment Date. Fractional Shares will be issued and carried out to three decimal places.

Minimum Purchase; Subscription Period

The minimum initial subscription per Investor is $1,000,000. The minimum subscription for additional investments by an Investor shall be $500,000. Shares are offered directly by the Fund. The minimum subscription amount and the minimum additional subscription amount may be reduced by the Board in its sole discretion. To subscribe for Shares, an Investor must submit a Subscription Agreement (in the form attached hereto) to the Administrator. Subscription Agreements and consideration for the

Shares subscribed to must be received by the Administrator at least five Business Days before the intended Subscription Date for the subscription. Upon acceptance of the subscription, capital contribution for the Shares subscribed must be transmitted immediately to the Fund's subscription account. Cleared funds must be in the Fund's account by 5 p.m. (Bermuda time) at least three Business Days before the Subscription Date . Consideration for Shares must be paid for in cash, although the Directors may in their absolute discretion accept other forms of payment.

Eligible Subscribers

Generally, except with respect to Qualified U.S. Persons (as defined in (b) below), the Shares will not be offered for sale in the U.S. or its territories or possessions or to nationals thereof, persons resident therein or entities established under the laws thereof. Shares will be offered from time to time on a private basis only to a select number of institutional and individual investors which meet applicable regulatory requirements. The Shares may be purchased only by (a) individuals that are not citizens or residents of the United States or entities that are not organized under the laws of the United States ("Non-U.S. Persons"), and (b) U.S. Persons within the meaning of the U.S. Internal Revenue Code of 1986, as amended (the "Code"), that are subject to the U.S. Employee Retirement Income Security Act of 1974, as amended ("ERISA"), or are otherwise exempt from payment of United States Federal income tax, or an entity substantially all of

the ownership interests in which are held by entities exempt from payment of U.S. Federal income tax ("Qualified U.S. Persons"). Prospective shareholders who are Qualified U.S. Persons must also qualify as "qualified purchasers" under §2(a)(51) of the Investment Company Act and "qualified eligible participants" under CFTC Regulation 4.7. Non-U.S. Persons and Qualified U.S. Persons that are Qualified Purchasers and Qualified Eligible Participants are hereinafter referred to as "Qualified Holders." Shares may not be purchased or held by or for the account of Bermuda residents. The Board of Directors may reject any subscription for any reason, or for no reason, in their sole and absolute discretion.

Series of Shares

In order to ensure a more equitable allocation of the Incentive Fee (see "Fees and Expenses" below) among Investors investing in the Fund at different times during the calendar year, Shares issued as of separate Subscription Dates will be designated as Shares of separate series (each with its own Net Asset Value per Share) as follows: Shares issued on the first Subscription Date of a calendar year will be designated as Series 1 Shares. Shares issued on Subscription Dates that do not fall on the first Subscription Date of a calendar year will be designated as Shares of a consecutive series of Shares. To the extent that there is no Loss Carryforward with respect to a Series, such additional series of Shares will be converted into Series 1 Shares at the beginning of each calendar

year as described in more detail under "FEES AND EXPENSES".

FEES AND EXPENSES

Organization and Offering Expenses

The aggregate initial organization and offering expenses will be advanced by the Investment Adviser and will be reimbursed by the Fund at such times and in such amounts as requested by the Investment Adviser. Provided that the Fund commences investing activities, the Fund may treat its organizational costs and expenses in accordance with U.S. Generally Accepted Accounting Principles, although it may elect to modify its treatment of such costs and expenses to accommodate its practical needs, including without limitation, by amortizing such organizational costs and expenses over a period of up to 60 months. Subsequent offering expenses will be direct expenses of the Fund.

Operating Expenses

The Fund will bear its routine operational expenses, including legal, custodial, accounting, printing, and audit expenses, expenses related to the investments of the Fund's assets, including, without limitation, brokerage commissions, investment related travel expenses, interest expense and professional and consulting fees relating to particular investments, insurance premiums (if any), administrative, directors fees and expenses, expenses incurred with respect to furnishing the Shareholders with annual reports and other financial information, the

Administrator's and the Registrar and Transfer Agent's fees and annual Bermuda government fees. The Investment Adviser will bear all of its general overhead expenses in connection with its services to the Fund (and the Master Fund), including employee salaries and office and equipment costs. The Fund will also, at such time as it becomes a member of the Master Fund, indirectly bear its allocable share of expenses incurred by the Master Fund, which will consist primarily of brokerage commissions and other operating and investment expenses paid by the Master Fund.

Investment Adviser Compensation

The Investment Adviser will receive a quarterly management fee determined at a rate equal to 1% per annum of the Fund's Net Asset Value, accrued monthly and payable in arrears as of the end of each calendar quarter. It also will receive a quarterly incentive fee (the "Incentive Fee") equal, in the aggregate, to 20% of the increase in Net Asset Value of each series of Shares over the sum of (i) the Series' Net Asset Value as of the commencement of each calendar quarter plus (ii) the yield on the Fund's portfolio at a rate equal to the yield of the Lehman Government Credit Index for such period (the "Hurdle"). A Series of Shares will only be charged with an Incentive Fee if its Net Asset Value at the end of a quarter (prior to accrued Incentive Fees), if any, for the quarter is greater than (i) its Net Asset Value at the time of its initial subscription (or the Initial Closing Date, whichever is later) or (ii) its Net Asset Value at the time the last Incentive Fee was

charged against such Series, whichever is higher, plus the Hurdle (the "High Water Mark"). In the event that the Fund invests in the Master Fund, the Investment Adviser will not be entitled to a separate management or investment advisory fee as manager of the Master Fund but will be entitled to reimbursement for expenses incurred on behalf of the Master Fund.

In order to ensure that the Incentive Fee is charged only to Shares that have appreciated in value since their acquisition and to make sure that all Shares have the same Net Asset Value, the Fund will issue different series of Shares to investors who invest at different times to ensure that the Incentive Fee is charged only to Shares that have appreciated in value. See "CHARGES TO THE FUND-Calculation of Investment Adviser Compensation."

Deferral of Fees. The Investment Adviser may elect, prior to the commencement of the Fund's trading activities with respect to its first calendar year of trading and prior to the commencement of each calendar year thereafter, to defer for a period of up to ten years payment of all or any portion of its Management Fees and/or Incentive Fees earned with respect to that subsequent period.

Administration

For its services as the Fund's Administrator, the Fund will pay the Administrator fees in accordance with the Administration Agreement.

Registrar and Transfer Agent
For its services, the Registrar and Transfer Agent will receive a fee of U.S. $2,500 per annum and is entitled to reimbursement of actual out-of-pocket expenses incurred on behalf of the Fund.

Directors' Fees
Each Director who is not an officer or employee of the Investment Adviser receives a flat annual fee of U.S. $2,000 for serving in such capacity. The Directors shall be entitled to reimbursement from the Fund for reasonable out-of-pocket expenses incurred by them on behalf of the Fund.

Trustee Services
The Trustee of the Purpose Trust holding the Management Shares will be entitled to an acceptance fee of $1,500 and an annual trustee fee of $1,500 payable by the Fund.

Custody and Prime Brokerage Services
For its services as custodian of the Fund's assets and prime broker of the Fund, the Fund will pay the Custodian in accordance with the Custody Agreement.

SHAREHOLDER INFORMATION

Limited Liability
Shareholders will purchase Shares in the Fund with limited liability and cannot lose more than the amount of their investment and profits thereon.

Redemption of Shares

Shares may be redeemed at a Shareholder's option at the Net Asset Value per Share of the relevant Series as of any Valuation Date upon at least 15 Business Days prior written notice to the Fund. The Fund may compulsorily redeem the Shares of any Shareholder on at least ten days' prior written notice to such Shareholder at the sole and absolute discretion of the Directors of the Company or where the holding of such Shares may result in regulatory, pecuniary, legal, taxation or material administrative disadvantage to the Fund or its Shareholders. There is no redemption charge or penalty. The Fund will generally pay 95% of the redemption price within 30 Business Days of the effective date of the redemption without interest, and the balance promptly at such time as the Fund shall determine, at the discretion of the Board of Directors.

The Fund expects to pay the entire redemption price in cash, although it has the right to distribute marketable securities. A redemption notice, once given, may not be cancelled or rescinded without the consent of the Directors in their sole discretion.

The Fund reserves the right to decrease, limit, delay or deny a redemption request, or any payment on a redemption request, if reasonably necessary in order to comply with the Fund's credit and other agreements, as well as for other reasons.

Transfer of Shares
There is no active secondary trading market for the Shares, nor is one expected to develop. Shares may not be sold, transferred or otherwise disposed of by a Shareholder in the United States or to any person corporation or entity which is not a Qualified Holder without prior written consent of the Fund and compliance with all applicable laws.

Favorable Tax Treatment
Under existing legislation in Bermuda, there are no income, capital gains or withholding taxes payable by the Fund or its Shareholders, nor are there any Bermuda estate, succession, or inheritance taxes payable by the Shareholders with respect to their Shares.

There is, at present, no direct taxation in Bermuda and interest, dividends and gains payable to the Fund will be received free of all Bermuda taxes. The Fund is an exempted company under Bermuda law and the Fund has made application to the Minister of Finance of Bermuda for, and expects to receive, an assurance that no law hereafter enacted in Bermuda imposing any taxes or duty to be levied on income or capital assets, gains or appreciation will apply to any income or property of the Fund.

The Fund and its Shareholders should not be subject to United States taxation as a consequence of the Fund's trading activities.

Dividends and Distributions

The Fund is a capital appreciation fund and does not intend to distribute dividends. Any dividends declared will be in the sole discretion of the Directors and will be paid out of the Fund's accumulated net income plus the net of accumulated realized and unrealized capital gains and accumulated realized and unrealized capital losses. Any dividends declared will be paid in accordance with Bermuda law.

Net Asset Value

The Net Asset Value of the Fund and each Series will be calculated at each Valuation Date in U.S. Dollars (unless the calculation at such Valuation Date has, for any reason, been postponed or suspended). Shareholders may, at any time, obtain information from the Fund regarding the most recently available indication of Net Asset Value.

ERISA Considerations

Fiduciaries and other persons investing in Shares in the Fund on behalf of employee benefit plans, employee retirement plans, individual retirement arrangements, Keogh Plans and other plans (together, "Plans") subject to ERISA or the Code should be aware that the assets of the Fund may constitute "plan assets" for purposes of the reporting, disclosure, prohibited transaction and fiduciary responsibility provisions of ERISA and the Code. The Investment Adviser qualifies as a "qualified professional asset manager" under applicable regulations under ERISA and will take all appropriate steps to ensure that the Fund does not

engage in any prohibited transactions under ERISA. The Investment Adviser will be a fiduciary of Plans investing in the Fund for purposes of ERISA. An investment in the Fund by Plan Investors requires special considerations, and fiduciaries of such Plans are encouraged to carefully review this Memorandum and the Section entitled "ERISA Considerations."

GENERAL

Auditors
Deloitte & Touche, Hamilton, Bermuda

Legal Counsel
Foley & Lardner, Milwaukee, Wisconsin, have counseled the Investment Adviser on various matters of United States law relating to the Fund. Appleby, Spurling & Kempe, Hamilton, Bermuda, have advised the Investment Adviser and the Fund 67a on various matters of Bermudan law relating to the Fund.

Custody Arrangements
The Fund is exempt under the Regulations from the requirement to appoint a Bermuda custodian of Fund Assets since the Fund is classified as a Bermuda Institutional Scheme. The Custodian will serve as custodian of the assets of the Fund.

Prime Broker
The Custodian will also initially be engaged as prime broker for the Fund, will function as clearing agent and will provide margin leverage and certain

valuation and reporting services to the Fund and the Administrator.

Reports
The Fund will provide Investors with monthly unaudited performance reports and annual audited financial statements prepared by the Fund's auditors.

Fiscal Year
The Fund's fiscal year will be the calendar year ending December 31st.

Conflicts of Interest
The Fund will be subject to certain actual and potential conflicts of interest. For example, the Investment Adviser will not be required to devote all of its time to the management of the Fund and the Investment Adviser has provided and expects to continue to provide investment management and advice to clients other than the Fund. In addition, the terms of the Investment Adviser's compensation from the Fund was not established by arm's length negotiations. See "CONFLICTS OF INTEREST."

Risks
Investment in the Fund involves greater risks than certain other types of investments. Investors in the Fund should be able financially to bear a loss of their investment. There is no assurance that the Fund will be profitable or will avoid substantial losses. "See Risk Factors."

RISK FACTORS

There is high risk associated with an investment in the Fund and an investment in the Fund should only be made after consultation with independent qualified sources of investment and tax advice. The following does not purport to be a comprehensive summary of all the risks associated with an investment in the Fund. Rather, the following are only certain particular risks to which the Fund is subject that the Investment Adviser wishes to encourage prospective investors to discuss in detail with their professional advisors:

The Fund Has No Performance History. The Fund has no performance history.

Reliance on the Investment Adviser. All decisions with respect to the Fund's assets and the general management of the Fund will be made by the Investment Adviser which relies on the services of several key employees, including without limitation, Mark D. Lay, Steven L. Sanders and Edward Adatepe. Shareholders will have no right or power to take part in the management of the Fund. As a result, the success of the Fund for the foreseeable future will depend largely upon the ability of the Investment Adviser and in particular Mark D. Lay, Steven L. Sanders and Edward Adatepe. Should any of these employees leave or become incapacitated for any period of time, profitability of the Fund's investments may suffer.

Achievement of the Fund's Investment Objective. No guarantee or representation is made that the Fund's Investment Objective will be successful. The Fund's investment program may include such investment techniques as short sales, leverage and limited diversification, which practices can, in certain circumstances, maximize the adverse impact to which the Fund's investments may be subject.

Eligibility to Engage in Futures Transactions. Certain transactions in commodity futures and options on futures and the investment and trading strategies associated with such transactions will not be available to the Fund unless and until the Investment Adviser has registered as a CPO with the CFTC. While the Investment Adviser has filed an application with the CFTC for licensing as a CPO, no assurance can be given that such license will be obtained and the Investment Adviser is not obligated to pursue or obtain any such license or registration.

No Current Income. The Fund's investment policies should be considered speculative, as there can be no assurance that the Investment Adviser's assessments of the short-term or long-term prospects of investments will generate a profit. In view of the fact that it is unlikely that the Fund will pay dividends, an investment in the Fund is not suitable for investors seeking current income for financial or tax planning purposes.

Currency Risk. Investments in securities of non-U.S. issuers will be denominated in currencies other than

the U.S. Dollar, and hence the value of such investments will depend on the relative strength of the U.S. Dollar. The Fund may be affected favorably or unfavorably by exchange control regulation or changes in the exchange rate between foreign currencies and the U.S. Dollar. Changes in foreign currency exchange rates may also affect the value of dividends and interest earned, and the level of gains and losses realized on the sale of securities. The rate of exchange between the U.S. Dollar and other currencies is determined by forces of supply and demand in the foreign exchange markets. These prices are affected by the international balance of payments and other economic and financial conditions, government intervention, speculation and other factors. Additionally, because the Fund's Net Asset Value will be calculated, purchased and redeemed in U.S. Dollars, each shareholder, and not the Fund, will bear the risk of any currency exposure resulting from differences, if any, in the value of the U.S. Dollar relative to the shareholder's reference currency.

Investment in a Master Fund. An investment by the Fund in the Master Fund may be affected by an investment by other funds in the Master Fund. In view of the fact that all expenses of the Master Fund would be shared pro rata among its investors, if other investors in the Master Fund redeem their interests, the possibility exists that the Fund would bear the burden of an increased share of the Master Fund's expenses. Moreover, investors with larger investments than others may outvote the smaller

investors to their detriment. (See "SPECIAL INFORMATION ON THE MASTER FUND/FEEDER FUND INVESTMENT STRUCTURE.")

Counterparty Risk. The Fund is subject to the risk of the failure or default of any counterparty to the Fund's transactions. If there is a failure or default by the counterparty to such a transaction, the Fund will have contractual remedies pursuant to the agreements related to the transaction. The Fund seeks to minimize the Fund's counterparty risk through the selection of financial institutions and types of transactions employed. However, the Fund's currency hedging transactions and other operational mechanisms designed to match the Fund's maturity requirements to cash flow may involve counterparty and other risk elements that may create unforeseen exposures.

Nature of Certain Investments. There is no limitation on the size or operating experience of the companies in which the Fund may invest, provided that such securities have a Standard & Poor's rating of B or better. Some small companies in which the Fund may invest may lack management depth or the ability to generate internally or obtain externally the funds necessary for growth. Companies with new products or services could sustain significant losses if projected markets do not materialize. Further, such companies may have, or may develop, only a regional market for products or services and may be adversely affected by purely local events. Such companies may be small factors in their industries and may face intense

competition from larger companies and entail a greater risk than investment in larger companies.

Risks of Special Techniques Used by the Investment Adviser. The Fund may invest using special investment techniques that may subject the Fund's investments to certain risks. Certain, but not all, of these techniques and the risks that they entail are summarized below. The Fund, in any event, is not designed to correlate to the broad bond market, and should not be viewed as a substitute for conventional fixed income investments.

Investments in Fixed-Income Securities Generally. The prices of the Fund's fixed-income securities respond to economic developments, particularly interest rate changes, as well as to perceptions about the creditworthiness of individual issuers, including governments. Generally, the Fund's fixed- income securities will decrease in value if interest rates rise and vice versa, and the volatility of lower-rated securities is even greater than that of higher-rated securities. Also, longer-term securities are generally more volatile, so the average maturity or duration of these securities affects risk.

Although the Fund's U.S. government securities are considered to be among the safest investments, they are not guaranteed against price movements due to changing interest rates. Obligations issued by some U.S. government agencies are backed by the U.S. Treasury, while others are backed solely by the

ability of the agency to borrow from the U.S. Treasury or by the agency's own resources.

The Fund is also subject to the risk that its investment approach, which focuses on a broad range of fixed income instruments, may perform differently than other funds which target specific segments of the fixed-income market or invest in other asset classes.

Risks of Leverage. Borrowing money to purchase securities may provide the Investment Adviser with the opportunity for greater capital appreciation and to extend or shorten the average duration of the Fund's portfolio but, at the same time, will increase the Fund's exposure to capital risk and higher current expenses. The use of leverage also increases the volatility of the Fund's portfolio by magnifying both increases and declines in the value of the Fund's assets.

Up to 150% of the Fund's assets, at the time of investment, may be leveraged *(i.e.,* the combined value of borrowings and short positions). If the Fund's assets decline in value or there are significant redemptions from the Fund, the Fund may be required to post additional collateral with the lender or liquidate assets to pay off its borrowings. Moreover, if the assets under management are not sufficient to pay the principal of and interest on the debt when due, the Fund could sustain a total loss of its investment.

Investments in Mortgage-Backed Securities. Mortgages underlying mortgage-backed securities may be paid off early, particularly in periods when interest rates are low, which makes it difficult to determine the actual maturity of such securities and therefore to calculate how they will respond to changes in interest rates. The Fund may have to reinvest prepaid amounts of lower interest rates. The risk of prepayment is an additional risk of mortgage-backed securities.

Short Selling. The Fund may sell securities of an issuer short. If the price of the issuer's securities declines, the Investment Adviser may then cover the short position with securities purchased in the market. The profit realized on a short sale will be the difference between the price received in the sale and the cost of the securities purchased to cover the sale.

The possible losses from selling short a security differ from losses that could be incurred from a cash investment in the security; the former may be unlimited, whereas the latter can only equal the total amount of the cash investment. Short selling activities are also subject to restrictions imposed by the various national and regional securities exchanges, which restrictions could limit the investment activities of the Investment Adviser.

Risks of Options Trading. In seeking to enhance performance or hedge assets, the Investment Adviser may purchase and sell call and put options on both securities and securities indexes. A securities index

measures the movement of a certain group of securities by assigning relative values to the securities included in the index.

Both the purchasing and the selling of call and put options contain risks. Although an option buyer's risk is limited to the amount of the purchase price of the option, an investment in an option may be subject to greater fluctuation than an investment in the underlying securities. In theory, the exposure to loss is potentially unlimited in the case of an uncovered call writer (*i.e.*, a call writer who does not have and maintain during the term of the call an equivalent long position in the stock or other security underlying the call), but in practice the loss is limited by the term of existence of the call. The risk for a writer of an uncovered put option (*i.e.*, a put option written by a writer that does not have and maintain an offsetting short position in the underlying stock or other security) is that the price of the underlying security may fall below the exercise price.

The effectiveness of purchasing or selling securities index options as a hedging technique will depend upon the extent to which price movements in assets that are hedged correlate with price movements of the index selected. Because the value of an index option depends upon movement in the level of the index rather than the price of a particular security, whether a gain or loss will be realized from the purchase or writing of options on an index depends upon movements in the level of prices in the securities market generally, rather than movements

in the price of a particular security. Successful use of options on indexes will depend upon the ability of the Investment Adviser to predict correctly movements in the direction of the market generally. This ability requires skills and techniques different from those used in predicting changes in the price of individual securities.

Risks of Futures Trading. Upon licensing of the Investment Adviser by the CFTC as a CPO and satisfaction of certain other conditions, the Fund may acquire commodities futures contracts and options on futures contracts.

Futures contracts and options thereon are highly volatile. Price movements of financial and interest rate futures and options thereon are influenced by a wide variety of factors, including, among other things, government, trade, fiscal, monetary and exchange programs and policies, national and international political and economic events and changes in interest rates.

When futures contracts are traded on United States exchanges, both buyer and seller are required to post margins with the broker handling their trades as security for the performance of their purchase and sale undertakings and to offset losses in their trades due to daily fluctuations in the markets. The low margin deposits typically required in futures trading (typically between 2% and 15% of the value of the futures contracts) permit an extremely high degree of leverage. Accordingly, a relatively small change in

interest rates or the price of a commodity can produce a disproportionately large profit or loss, which can exceed substantially more than the initial margin on a trade. The Investment Adviser intends to limit the Fund's initial margin and option deposits in connection with such futures contracts to not more than 10% of the Fund's assets.

Successful use of futures by the Investment Adviser is also subject to the Investment Adviser's ability to predict correctly movements in the direction of interest rates and other relevant financial markets, and to the extent a transaction is entered into for hedging purposes, to ascertain the appropriate correlation between the transaction being hedged and the price movements of the futures contract.

Swap Agreements. The Fund may enter into interest rate, index or currency rate swap agreements in an attempt to hedge against changes in interest or currency rates or index values exceeding minimum or maximum values. Most swap agreements entered into by the Fund would calculate the obligation of the parties on a "net" basis. Consequently, the Fund's obligations or rights on a swap agreement, and the risk of loss, would be limited only to the net amount to be paid or received based on the relative values of the positions held by each party.

Portfolio Turnover. Because the Investment Adviser will make changes whenever necessary, in its opinion, to take advantage of anticipated movements in the U.S. Treasury yield curve and/or inter-sector

spread relationships, it is anticipated that the Fund's portfolio will have a high turnover rate. Turnover of the Fund's portfolio may involve the payment by the Fund of dealer spreads or underwriting commissions, and other transaction costs, on the sale of securities, as well as on the reinvestment of the proceeds in other securities. The greater the portfolio turnover, the greater the transaction costs to the Fund which will reduce the Fund's total return.

Lack of Diversification. The Fund's portfolio may not be diversified among sectors, industries, geographic areas, duration or types of securities. In addition, the Fund's portfolio may not be diversified among a wide range of issuers. Accordingly, the Fund's portfolio may be subject to a more rapid change in value than would otherwise be the case if the Fund were required to maintain a wide diversification of its investments.

Acquisition of Illiquid Securities. Fund investments may include significant amounts of debt securities and other financial instruments for which no market or only a limited market exists (and which may even be restricted as to transferability under federal or state securities laws), and the disposition of such investments in the event of an unsuccessful outcome may be possible only at substantial discounts from their purchase price or intrinsic business value. The Fund's holding of illiquid securities may adversely affect the ability of Shareholders to receive redemption proceeds.

Incentive Fee Arrangements. The Investment Adviser could receive substantial compensation if it generates increases in Net Asset Value above the Hurdle for the Shareholders. Such compensation may provide an incentive for the Investment Adviser to effect larger and more risky transactions than would be the case in the absence of such arrangements. The Investment Adviser does not expect to modify or adjust its investment methodology in any way as a result of such incentive. The Investment Adviser may receive compensation with respect to unrealized appreciation of Fund assets as well as with respect to realized gains.

Advisers Act Prohibition. Section 205(a)(1) of the Advisers Act prohibits investment advisers, unless exempted from registering as an investment adviser under the Advisers Act, from providing investment advice for compensation "on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of [a] client." The Investment Adviser will provide investment advice to the Fund and will be compensated, in part, upon a share of the capital gains of the Fund.

In order to prevent a possible violation of Section 205(a)(1) of the Advisers Act, the Fund will seek to comply with Rule 205-3 (the "Rule") under the Advisers Act, which permits an investment adviser to collect fees on a capital gains basis if such advice is provided solely to "qualified clients" as defined under the Rule. Since all Investors must be "Qualified Purchasers" in order to invest in the Fund and a

Qualified Purchaser also satisfies the criteria for a Qualified Client, the Fund will be in compliance with the Rule.

The intended purpose behind the Advisers Act prohibition of such fee arrangements with clients (unless the client is a "qualified client") is the belief that this type of performance fee arrangement may create an incentive for the Investment Adviser to make investments that are riskier or more speculative than would be the case in the absence of a performance fee.

Non-Public Information. From time to time, the Investment Adviser may come into possession of material non-public information regarding a potential investment that limits the Investment Adviser's flexibility in buying and selling Fund investments. The Fund's investment flexibility may be constrained as a consequence of the Investment Adviser's inability to use such information for investment purposes.

Broker-Dealers. All orders for the purchase or sale of Fund investments will be placed on behalf of the Fund by the Investment Adviser. The Investment Adviser may negotiate the purchase of investments directly with the sellers or may utilize broker-dealers to execute transactions. In selecting broker-dealers, subject to applicable limitations of the federal securities laws, the Investment Adviser will consider such factors as size and type of the transaction, the nature and character of the markets for the security,

the quality of the execution and settlement services, the financial condition of the broker-dealer firm and the reasonableness of any commissions.

The Fund may execute portfolio transactions with broker-dealers who provide research and/or execution services to the Fund and/or other accounts over which the Investment Adviser or its affliates exercise investment discretion. The selection of such broker-dealers generally is made by the Investment Adviser based upon the quality of such research and/or execution services. In any case where the Fund is to pay higher commissions in recognition of such research and/or execution services, the Investment Adviser must determine in good faith that such commissions are reasonable in relation to the value of the brokerage and/or research service viewed in terms of a particular transaction for the Investment Adviser's overall responsibilities to the Fund or its other clients.

Custodial Risks of Broker/Dealers. Various broker/dealers will trade with the relevant exchange as a principal on behalf of the Fund, in a "debtor-creditor" relationship, unlike other clearing broker relationships where the broker is merely a facilitator of the transaction. Such broker could, therefore, have title to certain assets of the Fund (for example, the transactions which the broker has entered into on behalf of the Fund as principal as well as the margin payments which the Fund provides). In the event of such broker's insolvency, the transactions which the broker has entered into as principal could therefore

default and such assets of the Fund could become part of the insolvent broker's estate, to the detriment of the Fund.

Early Termination. In the event of the early termination of the Fund, the Fund would have to distribute to the Shareholders their pro rata interest in the assets of the Fund. Such an early termination would have the effect of accelerating the unamortized portion of any organizational fees, thereby decreasing amounts otherwise available for distribution. Certain assets held by the Fund may be illiquid and might have little or no marketable vale. It is possible that at the time of such sale or distribution, certain securities held by the Fund would be worth less than the initial cost of such securities, resulting in a loss to Shareholders.

Effect of Substantial Withdrawals. Substantial withdrawals by Shareholders within a short period of time could require the Investment Adviser to liquidate positions more rapidly than would otherwise be desirable, which could adversely affect the value of the Fund's assets. The resulting reduction in the Fund's assets could make it more difficult to generate a positive rate of return or to recoup losses due to a reduced equity base.

Regulation. The Fund is not registered as an investment company under the Investment Company Act (or any similar state laws). Registered investment companies are subject to extensive regulation. Investors, therefore, will not be accorded

the protective measures provided by such legislation. The Fund is governed by Bermuda law. Under Bermuda law, the Directors' principal duty is to act in the best interests of the Company. Shareholders may therefore not have the same statutory protection or remedies available under the laws of other jurisdictions.

Changes in Regulatory Requirements. The Fund's investments will be subject to various Federal, state and local regulatory requirements. Failure to comply with these requirements could result in the imposition of fines by governmental authorities or awards of damages to private litigants. Further, the Securities and Exchange Commission ("SEC") recently announced that it has commenced a review of "hedge funds" *(i.e.,* unregistered and unregulated investment entities like the Fund) to determine if it is necessary to enhance regulation of such entities for investor protection purposes. In the event that new regulations are adopted that require registration and/or impose other regulatory requirements under the securities laws for hedge funds, there can be no assurance that the Fund's operations would not be materially affected, in the form of increased costs and other regulatory requirements that could affect the potential return to investors in the Fund. There can be no assurance that these requirements will not require significant unanticipated expenditures by the Fund.

Conflicts of Interest. The Fund is subject to conflicts of interest. See "Conflicts of Interest."

Reserve for Contingent Liabilities. Under certain circumstances, the Board of Directors may find it necessary to establish a reserve for contingent liabilities or withhold a portion of the Shareholder's settlement proceeds at the time of redemption, in which case, the reserved portion would remain at the risk of the Fund's activities.

Risk of Litigation. The Fund may accumulate substantial positions in the securities of a specific company. Sometimes the Investment Adviser may engage in a proxy fight, become involved in litigation or attempt to gain control of a company. Under such circumstances, the Fund may be named as a defendant in a lawsuit or regulatory action and be subject to the costs involved.

Lack of Independent Experts Representing Investors. The Fund and the Investment Adviser have each consulted with counsel, accountants and other experts regarding the formation and terms of the Fund and the Advisory Agreement. The investors, however, have not been represented by such independent experts. Each prospective investor should consult his own legal, tax and financial advisers regarding the desirability of purchasing Shares and the suitability of an investment in the Fund. Foley & Lardner and Appleby, Spurling & Kempe are U.S. and Bermuda counsel to the Fund, respectively, and do not represent the prospective investors or Shareholders of the Fund.

Lack of Voting Rights. The Shares being offered participate in the profits and losses of the Fund but do not carry voting rights except under very limited circumstances. See "Statutory and General Information."

Limited Ability to *Liquidate Investment in Shares.* There is no public market for the transfer of Shares. A Shareholder may require the Fund to redeem all or any whole number of its Shares as of the close of business on any Valuation Date at their Net Asset Value. However, the right to obtain payment on redemption is contingent upon the receipt by the Fund of 15 Business Days' written notice, and the Redemption Price may differ significantly from the value of such Shares when redemption was requested. Requests for redemptions may not be withdrawn. The Fund may suspend any or all of the calculation of Net Asset Value, the calculation of Net Asset Value per Share and redemptions in the circumstances set out under "Redemptions and Transfers – Temporary Suspensions." The Fund may also temporarily suspend redemptions in order to effect an orderly liquidation of the Fund's assets necessary to effect redemptions.

The foregoing list of risk factors does not purport to be a complete explanation of the risks involved in an investment in the Fund. Potential investors should read this entire Memorandum before determining whether to invest in the Fund and

consult with their own financial and tax advisers. Potential investors should also be aware that, if they decide to purchase Shares, they will have no role in the management of the Fund, will not have any voting rights (except under very limited circumstances), and will be required to rely on the expertise of the Fund's Directors and the Investment Adviser in dealing with the foregoing (and other) risks on a day-to-day basis.

THE SHARES ARE SPECULATIVE AND INVOLVE A HIGH DEGREE OF RISK. THEY ARE SUITABLE ONLY FOR PERSONS WHO CAN AFFORD TO LOSE THEIR ENTIRE INVESTMENT. SHAREHOLDERS SHOULD READ THE MEMORANDUM AND ARTICLES OF ASSOCIATION AS WELL AS THE FUND'S CONTRACTS WITH SERVICE PROVIDERS WHICH ARE REFERENCED IN "STATUTORY AND GENERAL INFORMATION."

DETERMINATION OF NET ASSET VALUE

The Net Asset Value of the Fund shall be its assets less its liabilities, determined in accordance with United States generally accepted accounting principles ("US GAAP"), except that the Fund may elect to modify the treatment of organizational costs and expenses to accommodate its practical needs, including without limitation, by amortizing such costs and expenses over a period of up to 60 months. The Directors may, in their absolute discretion and where considered to be in the best interests of the

Fund, decide not to follow US GAAP. The Net Asset Value is calculated by the Administrator, on a quarterly basis, subject to the overall supervision of the Directors acting in good faith. The Net Asset Value of the Fund shall be the value of its gross assets less its gross liabilities (excluding accrued Incentive Fees) on any Valuation Date. The Net Asset Value Per Share as of any Valuation Day shall be the net asset value of those assets and liabilities of the Fund which are properly attributable to the Series of Shares of which that Share forms a part, divided by the number of Shares of the Series outstanding on that day.